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AIRLINE MERGERS, MONOPOLY, AND THE CAB

BY RICHARD J. BARBERT†

IN 1961 the eleven American trunk airlines reported an aggregate loss of \$34.8 million.¹ This elementary, but important fact (coming on the heels of a modest \$68,000 profit in 1960) sums up the various depressing forces that have been at work in the industry within recent years. The introduction of the jets, beginning in 1959, meant a substantial increase in capacity as well as large capital outlays. Total industry debt rose to more than \$1.3 billion, and interest payments alone climbed to \$59 million in 1961 (up from \$16 million in 1957). Passenger traffic, however, did not increase sufficiently either to fill the additional seats which had been made available or, even at higher fares, to offset the resulting increase in expenses. In 1960 revenue passenger miles carried by the trunk airlines grew by only 3.9%, in 1961 by 1.1%. By contrast, during these two years available seat miles increased by nearly 14%. As a result the passenger load factor was reduced to 56.2%. And, further, more passengers made use of coach-class service, some 57.8% of all passenger miles flown in 1961.

Between 1958 and 1961 total operating revenues of the trunk airlines increased by about a third (from \$1.5 billion to \$2 billion), but operating expenses advanced by about 44% (from \$1.4 billion to a little over \$2 billion). Earnings fell sharply in 1960 and went into the red in 1961. Naturally the rate of return on investments has fallen steeply, reaching 1.3% in 1961 (as defined by the Civil Aeronautics Board [CAB])²—far below the level officially considered reasonable and adequate (a year ago it was determined that for the trunk airlines a fair return on investment is 10.5%).³

Whether the economic situation of the industry is as bleak as some spokesmen suggest, however, and whether it is any more than a temporary condition that will be alleviated in large measure by improved circumstances beginning this year, are vital issues that have not been adequately appraised so far in the search for a remedy to what has simply been assumed to be a basic malady. At any rate, the agents of the larger airlines and the Chairman of the CAB, among others, have portrayed the plight of the industry in *El Greco* hues: all is dire, and something must be done soon if the industry is not either to flounder into bankruptcy or to require Federal subsidy again. Of what this action should consist, though, is not clear. A few advocates, such as the President of Continental Air Lines, feel that the proper step at this time is lower fares, an economy

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¹ Air Transport Association of America, *Facts and Figures About Air Transportation*, 16-17, 28 (23rd ed. 1962) [hereafter 1962 ATA Facts & Figures]. The other data contained in the opening paragraphs are also taken from this source. A more complete examination of the financial situation is contained in part I *infra*.

² Net income before interest and after taxes as a percentage of net worth and long-term debt.

³ General Passenger Fare Investigation, 1A Av. L. Rep. ¶ 21,236 (1961).

rate up to 25% below prevailing coach tariffs. The industry rather generally repudiates this approach to the problem (Continental at first withdrew its fare proposal, largely in response to the cold reaction it received from the CAB);⁴ most of the carriers, in fact, believe that higher fares are in order, designed so as to raise coach rates from 75% to 83-85% of first class rates as well as to boost the overall fare level.⁵ Their reaction thus is to boost fares and, apparently assuming little or no demand price elasticity,⁶ increase revenue enough to once more generate fair profits.

At root, however, the larger airline officials and their government counterparts feel that mergers provide the only real answer to the industry's needs (needs, I repeat, which are pictured as critical and otherwise incapable of satisfaction). In this quest they have received particular encouragement from Chairman Alan Boyd of the CAB. Speaking at Hartford last November, he expressed the "hope that others of the eleven domestic trunk lines now in existence will merge in the future. . . . Time may be running out for some carriers to receive what they and their investors consider to be a fair price for merging into other companies. It is altogether possible that financial conditions in the industry may become worse before they become better than they are now. Time is of the essence here, and there is little or none to waste."⁷ The same theme has run through several of his other addresses; in 1960 he said "it is entirely possible that a series of mergers or consolidations might be beneficial to the trunk-line industry and in the public interest."⁸ Again, in June of this year Chairman Boyd, perhaps with more reserve, stated that "in some situations it does appear that mergers may be accomplished that will save a great deal of expense and still provide the traveling public with a good transport system."⁹ One reporter concluded that these statements amount to an authoritative "carte blanche for airlines interested in merging."¹⁰

⁴ New York Times, Oct. 31, 1961, p. 61, col. 5.

⁵ For a review of the various airline positions, see New York Times, Nov. 16, 1961, p. 78, col. 4. Virtually all favor a general increase in fares, beyond the prevailing level (which incorporates a 3% increase placed in effect on February 1, 1962). Braniff and American are particularly strong advocates of narrowing the first-class coach differential. Eastern is in an anomalous position; although it criticized the Continental economy fare plan and generally favors higher fares, it has aggressively expanded its air-shuttle and air-bus services—both involving fares below coach levels. The CAB suspended the Continental economy rate, pending further study; then the airline withdrew its proposal. New York Times, Jan. 30, 1962, p. 46, col. 7. It resubmitted a similar plan later in 1962.

⁶ "Demand price elasticity" refers simply to the relative effect of a change in price on the quantity of the goods or service demanded. If price is raised 10% and demand falls by 10%, the elasticity is said to be -1. If demand does not change, elasticity is zero—a very uncommon situation. See generally Stigler, *Theory of Price*, ch. 3-4 (rev. ed. 1952).

⁷ New York Times, Nov. 4, 1961, p. 46, col. 1. History suggests that whenever the industry gets into financial difficulty the Board dashes forth with a bottle of merger medicine. In 1949 and 1950, just after a period of airline deficits, the CAB began a study looking to "the possibility, feasibility, and desirability of bringing about a merger of air carriers where such mergers would result in the improvement of the structure of the air transportation map of this country . . ." 1950 C.A.B. Ann. Rep. 2. See also its Statement of Policy Respecting Economic Program of 1949 for a similar expression favorable to trunkline mergers.

⁸ As quoted in *Public Utilities Fortnightly*, Sept. 14, 1961, p. 487.

⁹ New York Times, June 12, 1962, p. 51, col. 1.

¹⁰ New York Times, Feb. 4, 1962, § 10, p. 1, col. 6-8. On Sept. 28, 1961, Mr. Boyd met with the presidents of all the trunk carriers to discuss the economic situation and to compare their fare and rate "philosophy." It is believed that the Chairman may also have outlined his attitude to mergers; indeed, much of the trade discussion relative to this matter has been noted since the date of this meeting. *Aviation Week*, Sept. 18, 1961, pp. 38-39.

Whether that is true remains to be seen—and we shouldn't have too long to wait.

Prodded by the CAB and inspired by the businessman's inherent desire to reduce the vigor of the competitive struggle, several major airlines are actively engaged in the merger movement. Excepting the United-Capital merger approved in 1961 (which, because of Capital's bankrupt condition, places it in a distinct category), the most important of the mergers in process involves American and Eastern Air Lines, the second and fourth largest domestic carriers (together accounting for about a third of truck revenue passenger miles in 1961). Approval of their merger has already been formally sought from the CAB, and hearings have recently been concluded.¹¹ On June 19 the CAB authorized the Hughes Tool Company, which has legal title to 78% of TWA's stock, to acquire 56% of Northeast's common stock from the Atlas Corporation;¹² this brings a merger of these two lines one long step closer to realization, though it should be noted they are presently in close liaison since Northeast is using jet equipment leased from TWA for which it is not meeting current rental payments. And waiting in the wings, so to speak, are a number of other prospective consolidations. Precisely who will be involved in what marriage remains a subject for trade speculation. But the possibilities include a merger of TWA with Pan American (or with others, such as Delta or Northwest); of United with Western; and, among others, Braniff with Continental. Several observers of the scene contemplate a string of mergers that will produce five or six surviving trunk lines.¹³

Clearly, then, there is a trend to mergers among the trunk airlines, one that is certain to be accentuated greatly if the American-Eastern application is approved. What is distressingly unclear, however, is the need and desirability of the various consolidations that are contemplated. Perhaps they will have private advantage, though even here a question can be raised; but to the extent they do, there is likely to be serious public detriment. Competition will be reduced (and this quality has far greater utility than many commentators acknowledge) and the imbalance that prevails within the industry—with four carriers now accounting for over 70% of passenger traffic, the remainder divided among seven other participants—is perpetuated, if not actually emphasized. No doubt consolidation can produce some benefits, but in considerable measure these appear attainable without outright merger of the carriers themselves (the amalgamation of terminal facilities is one that comes immediately to mind).

At this point in the merger movement neither the carriers themselves nor their regulators have spelled out with any acceptable degree of precision the criteria that are relevant in appraising petitions for consolidation. In his Hartford speech last November, Chairman Boyd, after urging

¹¹ Hearings before the examiner finished on June 19. Post-hearing briefs were due on July 24 and rebuttal briefs on August 2. A decision is expected in the fall. *New York Times*, June 21, 1962, p. 48, col. 3.

¹² *New York Times*, June 20, 1962, p. 1, col. 2. The Board felt that the only alternative for Northeast (whose current liabilities exceed its current assets by over \$11 million on Nov. 30, 1961) was bankruptcy and possible reorganization, which it deemed unacceptable.

¹³ Robert Six, President of Continental Airlines, is of this opinion. *New York Times*, June 2, 1962, p. 34, col. 6. And the travel editor of the *New York Times* has outlined his plan for combining the various domestic airlines (including some of the local service operations) into about five systems. *New York Times*, Feb. 4, 1962, § 10, p. 1, col. 6-8; p. 19, col. 5. For a review of the trade rumors, see *Newsweek*, May 14, 1962, p. 88.

the airlines to consider more mergers, said "it is my personal view that if the carriers will not act soon in their own interests and in that of the public, the Board should institute studies of its own to develop detailed criteria for mergers and to determine what carriers should merge in the better interest of the industry and the nation."¹⁴ This is a bit like urging your son to go get married in order to solve his problems, but adding that the wisdom of marriage will have to be assessed subsequently. And it is a kind of cart-before-the-horse approach that is noticeable in other recent governmental pronouncements. The Project Horizon Report (of the Task Force on National Aviation Goals) spoke of airline mergers or "appropriate route adjustments" as "the only solution" to the economic plight of certain of the trunkline carriers;¹⁵ continuing, it declared that "mergers which result in strengthening marginal carriers, eliminating uneconomic competition, and providing new and/or improved service to the public should be encouraged." Yet after offering this vague comment, the Report *then* goes on to propose an "examination of future requirements and the creation of some standards for mergers."¹⁶ This is absurd; it makes little sense to recommend mergers as a solution for a problem, itself inadequately analysed, without first determining whether this treatment is efficiently related to the disease and whether other approaches might not offer substantially equivalent relief with less likelihood of public detriment. Perhaps the President recognized this, for in his April 5 message on "The Transportation System of Our Nation," he admitted that "this administration has a responsibility to recommend more specific guidelines than are now available and more specific procedures for applying them."¹⁷ Accordingly he appointed an interagency group¹⁸ to develop such criteria and to evaluate "each pending merger in transportation," having as one objective the maintenance of "effective competition" (undefined) "among alternative forms of transportation, and where traffic volume permits, between competing firms in the same mode of transportation."¹⁹ The ability of the group to translate these admonitions into concrete performance will be interesting to observe. At the moment, however, one is forced to the conclusion that key government officials are urging the airlines to consider merger but admitting they now lack the criteria to assess properly the merit of any given application.

While the regulators are lacking in a basis for their judgment, executives of the larger airlines, generally speaking, are confident that mergers offer the solution to their financial difficulties. While they admit that many factors are involved in their present plight, excessive competition is singled out as the real culprit. In its trial brief for the proceeding

¹⁴ New York Times, Nov. 4, 1961, p. 46, col. 1.

¹⁵ Federal Aviation Agency, *Report of the Task Force on National Aviation Goals: Project Horizon* 180 (Sept. 1961). The Chairman of the eight-man Task Force was formerly an official for two of the trunk airlines; the Vice-Chairman had been vice-president of the Air Transport Association of America; one of the other members was previously assistant general counsel for the Air Transport Association.

¹⁶ *Id.* at 181.

¹⁷ Message from the President of the United States, *The Transportation System of Our Nation*, H.R. Doc. No. 384, 87th Cong., 2d Sess. 8 (April 5, 1962).

¹⁸ A five-member committee has been appointed. It consists of the Secretary of Commerce for Transportation (Chairman), a member of the Council of Economic Advisers, an Assistant Secretary of Labor, the Assistant Attorney General for Antitrust, and the chief of the Justice Department's public counsel section. New York Times, May 16, 1962, p. 53, col. 6.

¹⁹ *Supra* note 17, at p. 8.

American Airlines says flatly "that the increased level of competition and the consequent inevitable provision of excess capacity is chiefly responsible for the industry's present state is clear."²⁰ Since 1955 the CAB has increased the degree of competition on most routes which formerly had provided the major carriers with cream for their operations. The effect has been to expose great chunks of the Big Four's previously monopolistic preserves to the competitive inroads of the smaller trunk operators. As American interprets it this increased competition is the principal cause of its (and the industry's) weakening position. Thus there is only one proper response: permit mergers to reduce this competition. Of course, it sees in merger other gains; facilities can be combined, flight equipment more efficiently utilized, and capital requirements significantly reduced. Consolidation hence will reduce competition and permit more effective and fuller exploitation of expensive equipment, with a consequent reduction in unit costs. In a nutshell, that is the heart of its argument. If true, the case for mergers is an impressive one.

Closer analysis, however, supports the belief that contemplated trunk airline mergers, specifically that between American and Eastern, are undesirable, unnecessary to the realization of operating economies, and poorly related to the industry's recent financial troubles. This is not to say that mergers, by curtailing competition, might not offer some indirect economic aid to the surviving airlines. What it suggests is that the price paid by the public, through the consequent reduction in competition and overall increase in concentration, is far too high.

Regardless of the conclusions reached, one fact, nevertheless, stands out: mergers cannot be intelligently appraised without a full appreciation of the relevant financial characteristics (the subject of part I), the structure of the airline industry, and the CAB's post-1955 efforts to increase the degree of competition over many routes and to achieve a lower level of concentration (part II). Only when these facts are digested can one sensibly evaluate the nature and implications of a specific merger—such as American-Eastern (part III). While the general conclusion of this article is that the case for airline mergers is unproven, part IV indicates that this is not a time for complacency on the part either of the airlines themselves or the CAB. Although carrier profits should turn up this year, if this does not happen and if more aggressive fare manipulation does not improve the situation, more drastic action may be required. Yet even if this requires some curtailment in competition (a point open to dispute), mergers do not appear to be the best way of achieving this goal.

I. ECONOMIC CHARACTERISTICS OF THE TRUNK AIRLINE INDUSTRY

As put forth by the proponents the case for airline mergers emanates from two principal hypotheses: *first*, that the trunk airline industry is in serious financial condition and cannot survive, absent basic structural reorganization or outside assistance; *second*, that mergers provide the best

²⁰ Trial Brief for American Airlines, In the Matter of the Application of American Airlines and Eastern Air Lines for Approval of Merger, CAB Docket No. 13355, p. 11. This theme runs through a number of exhibits which it presented. In particular, see exhibits AE-F, AE-151/155, 166-67. [All subsequent references to exhibits are to this same proceeding.] The parallel line of argument advanced by Eastern Air Lines is spelled out in its Merger Proxy Statement, March 12, 1962, *passim*.

solution to the industry's difficulties. This section deals primarily with the first of these two main arguments.

Viewed in broad financial terms the recent performance of the trunk airline industry has been highly disappointing. This was particularly true in 1961, though 1960 was not a great deal better. The surface indicia of this distress are easily recounted. While passenger capacity rose (on an available seat mile basis) by 7.4% in 1960 and by 6.9% in 1961,²¹ reflecting the high-rate of jet delivery and introduction into service (there are now about 300 four-engine jets in domestic use),²² passenger traffic increased only modestly. The number of revenue passenger miles flown in 1960 increased by 3.9% and in 1961 by only 1.1%. With increasingly more passengers flying by coach (in 1961 some 57.8% of all traffic carried), offsetting somewhat the higher fares which had been placed in effect, total operating revenue rose by only about 5% in 1961. Operating expenses increased somewhat more, and, in conjunction with nonoperating charges (notably interest on long term debt), total costs for the first time since 1947 ran ahead of revenues. The result: a net loss for the eleven carriers of \$34.8 million, down from the small \$68,000 profit recorded in 1960.²³ The return on investment (as that is defined by the CAB and the airlines)²⁴ declined from 2.8% in 1960 to 1.3% in 1961, far below what the Board determined in 1961 to be a reasonable return—namely, 10.5% for the trunk airlines as a group (10.25% for the Big Four, 11.125% for the rest.)²⁵ So described the situation is indeed dire.

But a look under the industry blanket reveals certain facts that somewhat brighten the scene. For one thing, about half of the 1961 deficit was accounted for by TWA, and most of its losses in turn were incurred through its international rather than its domestic operations.²⁶ Another \$9.5 million of the overall 1961 loss was reported by Northeast Airlines, which has been on the verge of bankruptcy for so long that its 1961 experience reflects no change in events. The fate of National Airlines, which for the fiscal year ending June 30, 1961, as a whole lost \$7.3 million, demonstrates further that the industry's losses were heavily concentrated in the first half of the year (roughly coinciding with the return of economic recovery).²⁷ As well, if the performance of these three airlines, along with Eastern's, is separated from the whole one finds that the other seven had a combined net profit of \$23 million.

²¹ 1962 ATA Facts and Figures 17.

²² 1962 ATA Facts and Figures 34. The number has increased rapidly, though it has slackened this year—for reasons that will be brought out later in the text. On Jan. 1, 1960, there were 84 four-engine jets in operation; by Jan. 1, 1961, the number had increased to 202. Forecasts called for a further increase to 301 by Jan. 1, 1962, and to 385 by 1963. Thereafter increases will be small—400 by the beginning of 1964. Federal Aviation Agency, Aviation Forecasts: Fiscal Years 1962-1967, table 3 (Oct. 1961). [There is some slight disparity as to the number of jets in service on Jan. 1, 1961, between the preceding source and Federal Aviation Agency, Statistical Handbook of Aviation 38 (1961 ed.).]

²³ For a more detailed breakdown of individual revenue and expense items, see 1962 ATA Facts and Figures 24-28.

²⁴ See *supra* note 2.

²⁵ See *supra* note 3.

²⁶ Braniff Airways, which operates flights to South America, is not unlike TWA in this respect. In 1961 Braniff recorded a profit of 67¢ a share on its domestic operations but lost 24¢ a share on its international service. Standard and Poor's Current Air Transport Survey, March 15, 1962, p. A27.

²⁷ National's new president and controlling stockholder estimates that for the current fiscal year the airline's operating revenues will be up by as much as a third compared with a year ago, and that pre-tax earnings will be \$2 a share. New York Times, June 21, 1962, p. 41, col. 2-3.

Moreover, any accurate assessment of the situation requires allowance for differences in the composition of the respective trunk airline capital structures. While the industry generally has added significantly to its debt since the arrival of the jet (debt made up about 29% of aggregate trunk airline capitalization in 1955; by 1961, excluding Northeast Airlines, it had increased to 66%),²⁸ this has been considerably more true of some of the airlines than of others. This story is told well by their widely varying debt equity ratios: American's is 2:1, Eastern's 1.95:1, TWA's a whopping 3.25:1, and for the smaller airlines much lower—1.3:1 for Continental and Delta, 1.1:1 for Braniff.²⁹ As a result their relative profitability—net profits as a percentage of net worth—takes on a distinctive hue. And even on an overall basis, if the net worth measure is employed, their earnings look much better than may otherwise appear. The reason is that the industry typically announces its rate of return on an investment base that consists of both equity *and* long-term debt. This in itself tends to over-emphasize the recent earnings downturn. In 1961, a lean year, several of the airlines made respectable returns on their common stock equity—Delta 11%, Northwest 8.5%, American 5%.

What customary industry financial reports hide, in particular, is the growing importance of interest and depreciation charges. These reflect the large additions of debt and purchases of jet equipment that have been made since 1955. Interest charges have skyrocketed over this period, rising from \$6.9 million in 1955 to \$58.6 million in 1961 (an increase of 850%, the largest of any single expense item). Also, as the jet equipment has been acquired, depreciation charges have mounted rapidly—up from \$102 million in 1955 to \$252 million in 1961. The relative magnitude of these cost increases is seen in this table:

TABLE 1. INCREASES IN TRUNK AIRLINE EXPENSES, 1955-1961

Expense Category	1955 (in millions)	1961	Percentage Increase
Total operating expenses	\$1,010	\$2,020	100%
depreciation	102	252	150
general services and admin.	409	794	94
maintenance	196	400	104
flying operations	303	574	90
Interest on long term debt	7	59	850

Source: 1962 *ATA Facts and Figures*, pp. 26, 28.

²⁸ Exhibit AE-D, appendix 18.

²⁹ Calculated from data in *Aviation Week*, May 14, 1962, p. 53. There is more than mere financial significance in the heavy debt loads assumed by the larger airlines. With a small group of banks and insurance companies having advanced most of the funds, the control they assume over contemplated mergers presents a dangerous situation. This is particularly true when the airlines and these financial groups tend indirectly to interlock through their boards of directors. When high airline officials of American, for example, sit alongside the spokesmen for Eastern on boards of directors of the financial institutions (e.g., Chase Manhattan Bank) which have advanced both airlines large sums of money and which must approve any merger, one has a right to be suspicious of the motives and circumstances leading to the decision to merge these two giant air carriers. This matter has been examined more completely elsewhere. See, A Staff Report to Subcommittee No. 5 of the House Judiciary Committee, *Proposed Merger of Eastern Air Lines and American Airlines*, 87th Cong., 2d Sess. 24-33 (1962). For a more colorful account see *Transport Workers Union of America, The Big Grab 3-9* (1962).

While depreciation is treated as an expense just like payments for jet fuel or wages, and has been rising much more rapidly than other cost components, it does not involve an actual cash withdrawal; rather it tends to depress earnings in a misleading fashion in the more recent years. Further, inconsistencies in depreciation rates greatly distort actual financial performance. As an illustration, in 1961 American and Eastern claimed about the same amount of depreciation, \$38 million. But Eastern is depreciating its jet equipment on the basis of an estimated useful life of 10 years and a residual value of 10%, while American is using 12 years and 15%.³⁰ On a hypothetical cost of \$100 this means that American is taking \$7.08 per year in depreciation (on a straight-line basis) as compared with \$9 in the case of Eastern. The effect is to depress Eastern's net earnings (or accentuate American's, if you prefer) and contributes heavily to the book losses it has claimed during the last two years. Indeed, according to one source, if certain changes in accounting practices which Eastern has adopted recently had been in effect during the period 1954-1956, its net earnings would have been in excess of \$50 million instead of the reported \$35 million.³¹

The pronounced increase in depreciation taken by the trunk airlines in the past three years means that corporate cash flow has been soaring enormously. As of September 30, 1961, their total retained earnings came to \$308 million, with aggregate depreciation adding about \$1.2 billion.³² The scale of these amounts can be gauged by comparing cash flow per share with earnings per common share for the year 1961.

TABLE 2. TRUNK AIRLINE CASH FLOW AND EARNINGS, 1961
(per common share)

<i>Carrier</i>	<i>Earnings</i>	<i>Cash Flow</i>
American	\$0.85	\$5.19
Braniff	0.43	3.05
Continental	0.40	3.80
Delta*	4.15	12.91
Eastern	(2.97)	13.60
National*	(3.92)	1.17
Northeast	(5.00)	(2.81)
Northwest	2.10	14.98
TWA†	(2.21)	6.49
United	0.70	12.85
Western	0.60	7.02

* Fiscal year ended June 30, 1961.

† Excludes special write-off.

Source: *Forbes*, May 1, 1962, p. 23

The growth of the companies' cash flow has many important implications.³³ It tends to reduce the practical significance of net earnings as an

³⁰ Eastern Proxy Statement, March 12, 1962, pp. 36, 43. For tax purposes depreciation is calculated at a faster rate.

³¹ Exhibit DL 30, p. 17 (presented by Delta Airlines).

³² 1962 ATA Facts and Figures 30.

³³ Of course, the great increase in cash flow has had general applicability (though typically it has been a good bit less pronounced than in the case of the trunk airlines). Corporate profits have not quite doubled over the last 15 years; but the total of retained earnings and depreciation

index to financial well-being. Corporations can literally live off their cash flow. At the end of 1966, for example, Eastern Air Lines could have working capital of over \$83 million—*after* paying cash of some \$200 million for 40 Boeing 727's that it has on order.³⁴ Even though this assumes that Eastern will make full use of its presently-indicated borrowing power, this still represents a sharp increase in its working capital, which amounted to \$18.6 million at the end of 1961. The explanation for this magical feat lies principally in the swelling depreciation charges it will be claiming throughout the period. Similarly, internally-generated cash will pay for Braniff's fourth Boeing 720 and for six BAC-111 short range jet transports to be delivered in 1964 and 1965.³⁵ Again the reason lies in depreciation charges; in 1963 these alone will amount to \$8.5 million, or \$3.75 million more than anticipated debt and interest payments.

With the trunk airlines having such substantial cash flow it is misleading to confine one's attention simply to the carriers' net earnings. This hides from view the very qualities that most financial students consider to be most important in assessing a firm's financial health. Actually the airlines, as well as most corporations, are a good deal better off than their profit claims indicate. This does not necessarily mean that airline earnings are now adequate, but it does suggest that their malady is not nearly so serious as at first appears.

If the airlines' 1960 and 1961 financial showing is indicative of future performance, however, there is nevertheless some cause for concern. But analysis of the situation suggests that the past two years were atypical and do not provide a useful guide to the future. There are many reasons for this conclusion. For one thing, the past five years have contained two sharp recessions, each roughly a year long. Both were severe and reflected a sizeable drop in the level of business activity. From 1957 to 1958 the Industrial Production Index fell by 7%; from January, 1960, to February, 1961, the Index fell by over 8%.³⁶ Since the airlines depend on business travel for the bulk of their revenue, it is only reasonable to suspect a correlation between the movements of the economic cycle and airline traffic. And increasingly this hypothesized relationship seems to be confirmed. Although during the two earliest postwar recessions, 1948-1949 and 1953-1954, traffic continued to increase substantially, this has not been true more recently. In 1958 revenue passenger miles did not increase at all over 1957 (when there had been a 13.6% increase). In 1959, with cyclical recovery, traffic rose sharply, by over 15%; but then with the return of recession in 1960 the rate of growth fell once more, so the passenger traffic rose by only 3.9%—and by only 1.1% in 1961 (a year only partially marked by an upswing).³⁷ Like most everyone else in the United States the airline industry has clearly been the victim of a low rate of economic growth and of increasingly shorter periods of

("cash flow") has more than doubled. Depreciation allowances now are equal to about 80% of plant and equipment expenditures compared with 33% in the late 1940's. Bookman, *The New Anatomy of Business Profits*, Fortune, May 1962, p. 107, 108-09.

³⁴ Exhibit DL 37B.

³⁵ Aviation Week, April 2, 1962, p. 35.

³⁶ Economic Report of the President, January 1962, table B-32; Jan. 1960, table D-29.

³⁷ 1962 ATA Facts and Figures 17.

recovery.³⁸ Its fortunes cannot be separated from the movements of the economy as a whole any more than those of the steel industry. When the economy is anemic, so too will be airline earnings.

But the failure of airline passenger traffic to grow more rapidly than it has since 1959 is attributable to more than economic recession. Fares have gone up sharply during the last four years, by about 25% (depending on the exact measure used) from 1958 through and including the 3% increase approved by the CAB this year. This is a point which the Air Transport Association, the certificated airlines' trade association, zealously attempts to disguise. But the fact remains that average revenue per passenger mile collected by the domestic scheduled airlines has increased by over 21% since 1958 as compared with a rise of only 3.4% in the Consumer Price Index.³⁹ Not unexpectedly this has meant increasingly more intensive use of coach class service and, it would also seem, a decline in the rate of traffic growth. Certainly it would be a terribly unusual market if demand were not to respond negatively to such steep price increases (airline spokesmen have a propensity for assuming, usually, that demand elasticity is zero; this is absurd, of course). The way in which airline fares have increased can best be illustrated as in the following table:

TABLE 3. ILLUSTRATIVE FARE INCREASES, 1954-1962
(one-way fares, tax excluded)

	New York-Los Angeles First Cl.	Coach	New York-Chicago First Cl.	Coach
July 1954	\$158.85	\$ 99.00	\$45.10	\$33.00
July 1957	158.85	99.00	45.10	33.00
July 1958	166.25	104.00	47.95	35.35
July 1959	166.25	104.00	47.95	35.35
Add for Jet	10.00	10.00	3.00	3.00
July 1960	171.45	109.15	50.15	38.30
Add for Jet	10.00	10.00	3.00	3.00
July 1961	171.45	109.15	50.15	38.30
Add for Jet	10.00	10.00	3.00	3.00
June 1962	176.60	112.45	51.70	39.45
Add for Jet	10.30	32.65	3.05	3.25

Source: *Official Airline Guide*

³⁸ Since many people consider the discussion of growth rates academic, it is well to note the close connection between rapid growth and high airline profits. From 1949 to 1955, a favorable period for the airlines, the economy (gross national product in constant 1954 dollars) expanded at an average annual rate of 5%. But from 1955 to 1959 the pace slowed to only 2% (and airline earnings, along with corporate profits generally, fell heavily). In 1959 the rate increased to 7%, and the trunk airlines earned nearly \$62 million. But then the rate of advance slowed again, to 2.9% (1960 compared with 1959) and then to 1.8% (1961 over 1960). Airline profits tumbled too. With the upswing now in progress earnings once more are advancing. Report of the Joint Economic Committee of Congress, Employment, Growth, and Price Levels, table 5, 86th Cong., 2d Sess. (1960); Economic Report of the President, January 1962, table B-3.

³⁹ Commenting on fares the ATA says, in carefully chosen public-relations type language, "the fare for travel on the U.S. scheduled airline system continues to be an outstanding bargain. The average 1961 air fare in the United States was 11.9% over the 1951 fare and just one penny per passenger mile over the average 1938 fare. While air fares increased just 18.8% on the average since 1938, the price of things generally, as measured by the consumer price index, increased 111.4%." 1962 ATA Facts and Figures 10. But if 1958 is used as the base year instead of 1938, then the average revenue per passenger mile has climbed from 5.64¢ to 6.28¢, up 21% compared with 3.4% in the consumer price index. Moreover, coach fares, from 1951 to 1961, have risen more than twice as fast as first class fares when figured on an average revenue per passenger mile basis. *Ibid.* This is even more true of short hauls than of longer hauls. See New York Times, March 11, 1962, § 10, p. 5, col. 3-4 (letter from an ATA vice-president).

Actually this table tends to understate the extent of fare increases; for example, in 1959, the major airlines operated a significant amount of propeller service between the points indicated, so that there was a real choice between jet and prop flights. This is no longer true; between New York and Los Angeles and New York and Chicago the principal carrier, American Airlines, offers nothing but jet service. The result is that the traveler who could go from New York to Los Angeles via coach prop equipment in 1959 for \$104 now must pay \$145.10.⁴⁰

With such steep fare increases it is not surprising that the airline passenger market has failed either to grow significantly in recent years or to reach a broader segment of the populace. Recent surveys indicate that roughly 80% of the American people have never traveled by commercial plane. And actually the airline passenger market is a good deal more limited than even this would indicate. A survey conducted by *Fortune* magazine showed that the 59% of passengers interviewed who were traveling on business accounted for 87% of the trips taken by all passengers. Moreover, "heavy business travelers" (those who took more than 31 air trips over a nine-month period) accounted for 80% of the trips.⁴¹ What this means obviously is that the airlines are concentrating the bulk of their attention on a very small segment of the potential market. Since business travelers are likely to be less responsive to fare increases (virtually all of this kind of expenditure is tax deductible, with a significant amount of it no doubt fully paid for by the taxpayers since it is chargeable to government contracts), it is probable that this is the only reason why the airlines have not sustained an actual decline in traffic growth over the past three years. Indeed the fact that traffic has continued to expand, though only slightly, in the face of the recent fare increases, actually appears to have kept the carriers themselves from recognizing that the market for airline travel is excessively constricted. At the core of the airlines' problem lies a lack of passenger traffic;⁴² certainly this will not be cured with continuing fare increases. Yet only Continental Air Lines has been "daring" enough to propose a sharp price cut—in the form of an economy service at 25% below coach rates. The rest of the industry believes in higher fares and in a narrower gap between coach and first class tariffs. This seems to be the ideal way to curtail traffic growth and to prevent enlargement of the market. Again, one wonders whether mergers are the answer to the industry's troubles, or whether the solution in fact doesn't lie within its own domain.

There are still other reasons why much of the blame for the trunk industry's recent performance can be laid at its own door. One of the superficial causes of the carriers' current difficulty is found in their extensive jet equipment acquisitions. Not only did this greatly increase available capacity, but it meant a sharp rise in debt and in related interest and depreciation charges. When orders for the four-engine jet equipment were

⁴⁰ The 5% round trip discount, in effect until 1959, has also been eliminated.

⁴¹ *Fortune Airlines Study*, p. 4. A similar study, conducted on behalf of American Airlines by the Opinion Research Corporation, showed that 78% of the American people have never flown on a commercial airline and that the 15% of air travelers who take five or more trips a year account for 64% of total air trips. *Aviation Week*, Feb. 26, 1962, p. 47. On the passenger travel market, generally, see Cherington, *Airline Price Policy* 30-41 (1958).

⁴² If the passenger load factor had been just one point higher in 1961 than it was (57.2% instead of 56.2%), gross revenues would have increased by about \$32 million.

being placed in 1956 (deliveries began in 1959) one business analyst concluded that the purchases were unjustified by predicted passenger traffic increases. In fact, concluded this writer, if traffic were to grow as was predicted and if all then-existing passenger equipment were kept in use and if the jet equipment were operated as many hours as the old equipment with seating space divided equally between first and coach class, the 1961 load factor would have been 38%.⁴³ As it turned out the actual load factor was 56.2%, reflecting, not a rise in traffic (indeed the 1956 traffic projections were highly accurate), but the earlier retirement from passenger service of piston equipment, slower than anticipated jet deliveries, and less intensive utilization of the new planes. The major trunk lines, American in particular, jumped into the jet market with near-reckless abandon (the President of American Airlines, C. R. Smith, appears now to recognize this).⁴⁴ The smaller carriers were more cautious, and Continental, for one, believes that if more efficiently used, American could operate with ten fewer 707's and 720's than it had in 1961 (as of March 5, 1962, American owned 48 planes of these types).⁴⁵ Whether this be true or not, it is clear that in purchasing the larger and far more expensive jet equipment the airlines took a considerably more optimistic view of the market than was warranted. (It is rather interesting now to note the gloomy outlook foreseen by American and Eastern executives; they appear to oscillate between all-out optimism when new jet equipment is ordered and full-scale pessimism when mergers are being pressed.)

In addition, the new equipment has been used to provide as frequent service as was the case when piston planes were in use, despite their capacity differences (in terms of size and speed). The carriers argue that ticket sales correlate to the number of flights offered and not to the capacity of the aircraft. Result: proportionately more flights are now offered with the larger, faster jet planes than with the older, smaller, slower piston planes. Given only a modestly expanding demand the effect obviously is a declining load factor.

There are a number of other factors that make the 1960-1961 performance a poor basis for predicting future airline industry financial results. Strikes in both years seriously affected several of the trunk carriers, taking a particularly heavy toll in the case of Eastern and TWA. The large-scale work stoppage in February, 1961, resulted in an overall revenue loss for the industry of \$12 million, equal to about a third of the aggregate deficit for the entire year. Accompanying these revenue curtailments have been certain special expenditures. The most serious of these stemmed from the necessity of modifying the Electra; this took several months and in the interim the plane had to be operated at suboptimal speed, with the effect of sharply increased operating costs (up from 168.7¢ per mile in the first quarter of 1960 to 191.7¢ in the second quarter). Eastern Airlines, which had 39 Electras in service, was especially hard hit; in fact all of its planes were not back in service until mid-Summer 1961. The Electra difficulties, of course, also affected the revenue side of the picture, creating what the airlines insist was anti-flying sentiment among

⁴³ Saunders, *The Airlines' Flight from Reality*, Fortune, Feb. 1956, p. 91. Said this writer: "Bluntly, there is no visible prospect of any such rapid increase in airline passenger traffic." *Id.* at 222.

⁴⁴ As reported in *Forbes*, May 1, 1962, p. 23.

⁴⁵ Exhibit CAL-R15.

many passengers. (Like so many airline claims this one lacks any acceptable degree of specificity; but no doubt it contains some truth.)

While the trunk airlines' financial problems in the last few years are less serious than may appear at first reading, admittedly there are some legitimate bases for concern; even so, so many factors have been at work during 1960 and 1961 that it is difficult to pinpoint the causes of their troubles. Some have been uncontrollable and unpredictable (labor disputes, accidents, equipment problems); others have been related to general economic circumstances; some appear to lie largely within their own control (rate increases that have chilled market development). A paramount question remains, however. Will the near-future be any more favorable to the airlines and can earnings reasonably be expected to increase in the years immediately ahead?

There are several reasons for believing that airline profits can be expected to turn up in the very near future. Jet operating costs have begun to decline, offering clear promise that they will be the most efficient operating flight equipment in airline history. In 1961 the total direct costs (including depreciation) of operating the Boeing 707 averaged 176.99¢ per revenue mile and for the Douglas DC-8 181.55¢ per revenue mile;⁴⁶ both cost levels were down from the prior year, bearing out the industry view that it takes a period of experience before new equipment can be operated most economically (in fact the DC-8 figure noted above represents a decline from 201.90¢ a year earlier, shortly after this type of equipment had been introduced into service). The great economy of the jet can most readily be appreciated by comparing it with, say, the Electra; the latter's 1961 per revenue mile cost was 160.91¢, or a little less than the pure jets. But the Electra has only 66 seats compared with 107 for the Boeing 707 and 117 for the Douglas DC-8 (these being American Airline seating configurations). The jet's seat mile costs are thus much lower, and promise to decline still more, making it extremely probable that the 1961 industry breakeven load factor of 56.5% will fall noticeably in 1962. There are, in addition, other kinds of costs related to the introduction of the jet that are now out of the way—introductory costs of flight simulator devices, repair equipment, etc. From now on the full advantage of the jets can seemingly be exploited.

Moreover, 1962 represents a hiatus in jet equipment deliveries, promising therefore not only a decline in the rate of increase in capacity but also a gradual slowing in added depreciation charges. As of June 20, 1961, some 94 Boeing 707's (the first four-engine jet in service) had been delivered, with 16 more on order for delivery in fiscal 1962 (several of these were actually delivered in calendar 1961) and fiscal 1963; the major airlines (with the exception of TWA) tend to have completed their 707 acquisitions. (American is in this category for example, presently awaiting some Convair 990's and the short and medium-ranged 727, scheduled for fiscal 1964.)⁴⁷ Likewise with the Boeing 720: fifty of these were in service on June 30, 1961, another 42 were on order for delivery in fiscal 1962, and only three are on order for later delivery.⁴⁸ Few of the Douglas DC-8's, although somewhat longer coming into production, remain to

⁴⁶ Aviation Week, March 13, 1961, p. 147; April 30, 1962, p. 55.

⁴⁷ Eastern Proxy Statement, March 12, 1962, p. 22.

⁴⁸ Federal Aviation Agency, Aviation Forecasts: Fiscal Years 1962-1967, table 2 (October 1961).

be delivered. While some other models still are being currently put in use (e.g., the Convair 990), the great bulk of jet equipment that has been ordered is already in service; 1962 and probably also 1963 will find few deliveries; and the next flurry of jet equipment deliveries will not come until 1964 (or thereabouts) when the three-engine Boeing 727 comes into full production. That, however, will still represent less of a burden than has been sustained during the last three years; American Airlines, for instance, has 25 Boeing 727's on order, but it already has possession of 48 four-engine jets and expects delivery of 16 Convair 990's within the next year or so; thus the 727 should pose a relatively smaller problem than has already been confronted.

The timing of jet plane deliveries and the consequent increase in capacity can be gauged from Eastern Air Line's projection of available seat miles:⁴⁹

1961.....	9,384 million (actual)
1962.....	10,425
1963.....	10,637
1964.....	10,875
1965.....	12,225

Eastern, which was tardy in acquiring the jets, thus will have a sizeable increase in capacity this year. But in 1963 and 1964 capacity will increase very little (for most of the trunk airlines the schedule is similar, with the significant exception that 1961 represented their large jump in capacity with 1962 to 1964 to be years of small gains—this reflecting their earlier entry into the jet race). When the Boeing 727 comes into production and deliveries begin there will be another sharp rise in passenger capacity. It deserves emphasis, though, that that is two to three years away and at the moment the airlines are in a position where traffic can begin to catch up with available supply.

But will passenger traffic increase sufficiently to permit fully profitable use of the existing jet capacity? That, of course, is a major question. From 1953 to 1957, years of substantial airline profits, traffic grew annually at rates of anywhere from 13% to 19%. As mentioned earlier, growth in the years following was cyclical, with the traffic increases during 1960 and 1961 being mediocre. As has been suggested there are many reasons for contending that the past two years were not fairly representative of future market development, in part because of economic recession and in part because of steep fare increases. With the upward turn of the cycle there is excellent reason for believing that traffic will again increase substantially. The Federal Aviation Agency (FAA) estimates that by the fiscal year 1965 domestic scheduled airline passenger traffic will amount to 41.5 billion passenger miles (this includes local service as well as trunk carriers and is up from 30.5 billion miles for fiscal 1961). Disaggregated, the FAA forecast indicates a 1.5 billion mile increase in fiscal 1962 (up about 5%), 3.0 billion in fiscal 1963, and 3.0 in fiscal 1964.⁵⁰ This reflects a presumed slower rate of growth than was experienced before 1957 (or in the single year 1959), but is well above that established for 1958, 1960, and 1961. The CAB itself is even more optimistic, predicting

⁴⁹ Exhibit DL-R 116, p. 2.

⁵⁰ Federal Aviation Agency, *Aviation Forecasts: Fiscal Years 1962-1967*, table 1 (October 1961).

that by 1965 the scheduled airlines will fly about 52.5 billion revenue passenger miles, with a particularly steep traffic increase in 1962.⁵¹

These projections of substantial passenger traffic increases appear to be borne out by actual 1962 performance. Revenue passenger miles flown by the domestic trunklines increased by 11.5% in January, 1962, over the same month a year earlier; in February, up 28.7% (this is somewhat distorted because of a labor stoppage in February, 1961); in March, up 9.6%; in April, up 11.5%; and in May, up 11.7%.⁵² Most of the airlines are forecasting substantial increases for the entire year, ranging from 6% to as high as 15%.⁵³ Certainly on the basis of results for the first five months of the year the future looks promising.

Officials of American Airlines, the principal proponent of mergers in the industry, however, strive to perpetuate the impression that bankruptcy (or a need for subsidy) is just around the corner. One financial source has taken note of this consciously pessimistic tone and says frankly that it is explained by their "commitment to the proposed merger."⁵⁴ Indeed, it is crucial to American and Eastern's position that they convince the appropriate parties that the industry's financial prospects are dim and that improvement cannot be expected through such forces as normal traffic increases, fare modifications, etc. If they are able to accomplish this feat it will merit an Oscar.

The case for airline mergers, as set forth by American and Eastern, is also premised on the ground that mergers will curtail unnecessary competition, improvidently brought about by the CAB since 1955, that has seriously depressed earnings to the economic detriment of the industry without consequent benefit to the public. Since this is a vital link in their position it deserves independent consideration, giving due weight to the structure of the industry and to policies of the CAB as they are reflected in route awards made since 1955.

II. THE NATURE AND IMPLICATIONS OF INCREASED AIRLINE COMPETITION

In the view of American Airlines, and the other principal proponents of large-scale trunk line mergers, the basic explanation for the industry's recent poor financial showing is excessive competition. Pointing to the large number of awards made since 1955 by the CAB which have increased the degree of competition, American contends that the additional industry expense annually attributable to this change in circumstance amounts to about \$200 million.⁵⁵ If competition could therefore be curtailed, and American claims that the best way of accomplishing this is

⁵¹ 1962 ATA Facts and Figures 20.

⁵² *Aviation Week*, May 21, 1962, p. 40; *Wall Street Journal*, May 16, 1962, p. 9, col. 3; *New York Times*, June 17, 1962, § 1, p. 83, col. 2. In May the passenger load factor was 51.3%, compared with 54.6% a year earlier.

⁵³ Actual results tend to confirm these prognostications. During the first quarter this year American Airlines' revenues increased by 17% over the year before. Over the first four months of 1962 Braniff's traffic rose by over 12% (in terms of revenue passenger miles flown). During the first five days of June Eastern flew 15% more passengers to Miami than in the same period last year.

⁵⁴ *Forbes*, May 1, 1962, p. 22.

⁵⁵ Summing up its position American Airlines' witness R. E. Kimble concludes that "the increasing spread and intensity of competition among the trunklines has been the primary cause of their decline in profitability. Competition has caused a rise in costs which has exceeded the increase in fares." Exhibit AE-F, p. 17. The \$200 million estimate is found in exhibit AE 166, p. 1.

via a series of mergers, profits would rise sharply and once more provide the various surviving carriers with an adequate return on their investment. So goes the argument.

Bolstering the case for mergers is the position of certain commentators that competition within a regulated industry, like airlines, is "senseless" anyway and without public advantage. "Airline competition," according to the travel editor of *The New York Times*, "is a kind of Twentieth Century myth, since where it counts—in price—domestic aviation is a monopoly with the price fixed by the Civil Aeronautics Board."⁵⁶ Accordingly, goes the argument, why should competition between rival carriers (certainly between more than two on any given route) be tolerated; it offers no real benefit and only increases airline costs.

To appraise these positions and to assess meaningfully the conclusion they are supposed to support, it is necessary to review some basic facts concerning the character of the airline industry and then consider the recent policies of the CAB.

A. Character Of The Industry

The domestic airlines, under federal administrative regulation since 1938, fall into four distinct categories—the trunk carriers, now eleven in number (representing through merger and abandonment a decline from the 23 originally certified); the local service, or feeder, airlines, now 13 in number (also representing a reduction from the 23 which have been authorized to provide service by the CAB in the years since 1938); the irregular, or nonscheduled, carriers; and the domestic all-cargo lines.⁵⁷ This article is concerned almost exclusively with the situation of the trunk carriers, which continue to provide the great bulk of domestic passenger service. It might be useful to note however, that the local service airlines are growing far more rapidly than the trunk lines; from 1955 to 1961, for instance, the feeder lines increased their revenue passenger miles by 190%, whereas the trunk lines traffic increased by only about 52%. The feeder carriers are profiting both from a sheer increase in traffic between the communities they always served and also from new routes which they have been granted (between 1951 and 1961 their route system has nearly doubled, now serving 580 cities compared with 384 a decade ago).⁵⁸ The trunk airlines continue, though, to provide most of the nation's passenger service.

In 1961, of a total of about 31 billion revenue passenger miles flown, the eleven trunk carriers accounted for 29.5 billion. In terms of structure the airline industry is a fine example of oligopoly—that is, a context in which a few firms supply the relevant service. In 1961 the

⁵⁶ New York Times, Feb. 4, 1962, § 10, p. 1, col. 6-8. There are others in the anti-competition camp: Tipton & Gewirtz, *The Effect of Regulated Competition on the Air Transport Industry*, 22 J. Air L. & Com. 157 (1955) (this reflecting the ATA attitude, with which the authors were associated and of which Mr. Tipton is now president); Bluestone, *The Problem of Competition Among Domestic Trunk Airlines*, 20 J. Air L. & Com. 379 (1953), 21 J. Air L. & Com. 50 (1954).

⁵⁷ An excellent portrayal of the domestic airline passenger industry may be found in Report of the House Judiciary Subcommittee, Airlines 8-33, 85th Cong., 1st Sess. (1957). Also see Fulda, *Competition in the Regulated Industries: Transportation* (1961); Gray, *The Air Transport Industry*, in Adams, *The Structure of American Industry*, ch. XII (rev. ed. 1954).

⁵⁸ Air Transport Association of America, *America's Local Service Airlines* (mimeo. May 10, 1962).

Big Four carriers accounted for about 73% of all the revenue passenger miles flown by the trunk lines. A complete breakdown is presented below:

TABLE 4. DOMESTIC TRUNK CARRIERS'
REVENUE PASSENGER MILES, 1961

	<i>number</i> <i>(millions)</i>	<i>percent</i>
All Domestic Trunk Carriers, Total	29,704	100.0
United	7,496*	25.0
American	5,965	20.1
TWA	4,287	14.4
Eastern	4,007	13.5
Total, Big Four	21,755	73.0
Delta	2,189	7.4
National	1,137	3.8
Braniff	1,070	3.6
Northwest	1,025	3.5
Continental	902	3.0
Western	874	2.9
Northeast	752	2.5

* Includes Capital

Source: Table 7 *infra*.

Compared with others, the airline industry is very highly concentrated—more so, say, than steel, drugs, electrical equipment, or chemicals.⁵⁹

A more accurate picture of the extent of concentration in the trunk industry, however, can be gained only by examining the characteristics of service along particular routes. This leads to several general observations. First of all, most of the routes connecting most of the 580 cities that receive scheduled airline service are monopolized; only one carrier provides the service, if indeed anyone does (obviously not all points receive service to all other points other than through interchange). Second, on most competitive routes only two carriers are involved, of which typically one is dominant. Third, only on a comparatively few, but quantitatively more important routes, are there three or more competing carriers; even here rarely are there more than three earnest rivals. Between New York and Chicago, for example, of the six airlines providing service, three carry 96% of the traffic, with American accounting for 43% and United for another 37%. Even on the most heavily authorized route in the country—New York-Washington, where eight lines can offer service—four carriers account for virtually all of the traffic, with two (American and Eastern) composing nearly 70% of the total. Below is presented a chart which indicates the highly concentrated character of a number of selected, high-density routes.

⁵⁹ For a presentation of concentration data in a number of manufacturing industries, see Kaysen and Turner, *Antitrust Policy* (1959), statistical appendix tables 1, 4. A more comprehensive listing, though less refined, is in a Report of the Senate Antitrust Subcommittee, *Concentration in American Industry*, 85th Cong., 1st Sess. (1958). Kaysen and Turner, interestingly, term airlines a highly concentrated industry—"still oligopolistic but significantly less concentrated." *Id.* at statistical appendix table 6, p. 290.

TABLE 5. DIVISION OF TRAFFIC AMONG AIRLINES ON SELECTED DOMESTIC ROUTES, 3d QUARTER 1961

Route	share of traffic carried by		
	One Carrier	Two	Three
New York - Boston	48%	73%	91%
Los Angeles - San Francisco	62	92	99
New York - Chicago	43	80	96
New York - Washington	43	70	86
New York - Miami	44	77	99
New York - Los Angeles	43	81	99
New York - Detroit	60	86	88
New York - San Francisco	38	71	99
New York - Cleveland	94	*	*
New York - Pittsburgh	49	95	*
Chicago - Los Angeles	33	57	79
Las Vegas - Los Angeles	60	75	83

* Insignificant

Source: CAB. Competition Among Domestic Air Carriers, 3d Quarter 1961.

On either basis, therefore, taking the trunk line industry as a whole or on specific routes, a very high level of concentration is indicated. And, with comparatively few exceptions, the dominant carriers are the properly-named Big Four—United (which became the largest through its recent merger with Capital), American, TWA, and Eastern (see table 4). The reason for their prominence (their relative magnitude has not changed greatly since 1938) is primarily attributable to the fact that they serve more of the larger traffic-generating cities. In 1960, the FAA classified 23 cities as so-called large traffic hubs; these accounted for 67.5% of all airline passengers. (Another 35 medium traffic points accounted for an additional 18.4%).⁶⁰ Of the 23 large traffic locations American Airlines, for example, serves 16 (including such major points as New York, Chicago, and Los Angeles) and is authorized to provide service between most of them. Indeed, of the top 58 traffic-producing communities in the United States, American Airlines serves 40. This is the key to its position and to the similar status of the other members of the Big Four: routes connecting a large number of the major traffic junctures which they have held since the first days of regulation under "grandfather" certification.⁶¹

In view of the intense concentration that pervades the trunk airline industry, and the various specific route segments, is there then any meaningful degree of competition? Put another way, with concentration so high does it make any sense to strive for maintaining competition? Some writers would answer in the negative, placing particular stress on the

⁶⁰ The Project Horizon Report puts the matter a little differently: "Domestic air passenger traffic presently is concentrated at relatively few of the 580 cities served. In 1960 the 25 leading traffic centers alone originated and terminated about two-thirds of all the domestic passenger-miles flown, and about 75 per cent of all the domestic passengers carried. Further, the first 100 cities accounted for more than 90 per cent of both passenger-miles and passengers." *Supra* note 15, at 180.

⁶¹ "The nature of the routes of the Big Four carriers, of course, gives them opportunity to develop large traffic volumes by tapping major pairs of metropolitan centers, particularly those of long-haul characteristics where air travel has more distinct time advantages over surface travel." Hearings before the House Antitrust Subcommittee, Monopoly Problems in the Regulated Industries: Airlines, 84th Cong., 2d Sess. (1956), vol. 1, p. 508.

fact that the industry is regulated (and perhaps also reflecting limited faith in the virtues of competition). The facts, however, point in just the opposite direction, suggesting strongly that competition retains substantial value even in this particular context. Admittedly in concentrated markets one does not find the kind of uninhibited competition that exists in, say, the garment industry. Here, where Chamberlin's "monopolistic competition"⁶² reigns, the rival sellers are aware that their actions will affect their compatriots and are thus unlikely to go without response, just as if General Motors lowers the price on the Chevrolet, Ford can be expected to follow suit. Thus in considering any "competitive" step any one of the firms must anticipate not only the market's response but also the reactions of its rivals. Inevitably this leads to a kind of tacit collusion, or spontaneous coordination.⁶³ And the airline industry provides a good example. By and large fares are uniform (they needn't be, for the CAB does not set fares, as some writers appear to think, it only responds to proposals made by the carriers), plane departures for the same destinations are scheduled at about the same time during the day, flight equipment is substantially identical, etc.

Nevertheless, as studies of the airline industry over the post-war years have amply established, competition, even within the limits which exist, has resulted in a number of innovations that have had distinct public benefit.⁶⁴ This has been particularly true in the case of equipment introduction; being the first in service with a better, faster plane has represented a competitive advantage eagerly sought—something which is unlikely to have been true absent the competitive spur. The American-United equipment rivalry is illustrative.⁶⁵ In 1946 American Airlines, for example, was the first to put the Convair model 240 in service (a definite improvement over the DC-3). United soon countered with the initial acquisition of the Convair 340. But American placed the initial order for the DC-7 and made first use of the Lockheed Electra (which, though ill-fated, permitted flights at average speeds in excess of 400 mph). In 1955 the two carriers again competed vigorously in jet acquisitions.⁶⁶ American gambled by ordering the Boeing 707 while United waited for the Douglas DC-8, with the result that American had jets in service before United. The latter, however, was the first to place an order for a medium-range jet, arranging to purchase the French-made Caravelle.

The advantages of competition are also discernible in the case of coach class service.⁶⁷ United had first provided coach flights between Los Angeles and San Francisco in 1940, but shortly abandoned the endeavor for fear that it would divert passengers from first class. Likewise, American's president spoke warmly of coach service in 1945. Yet it was neither of these large airlines that inaugurated coach flights. Instead it was Capital

⁶² Chamberlin, *The Theory of Monopolistic Competition* (7th ed. 1956). Through Chamberlin's emphasis is on product differentiation as distinct from structural oligopoly, the qualities are both involved in the airlines situation.

⁶³ See Fellner, *Competition Among the Few* (1949) for a more complete description of the processes of oligopolistic interdependence.

⁶⁴ Generally, Richmond, *Regulations and Competition in Air Transportation*, ch. IV (1961); Gill and Bates, *Airline Competition*, ch. II (1949) *passim*.

⁶⁵ Many of these episodes are examined in Stryker, *There's More Than One Way to Run an Airline*, *Fortune*, October 1961, p. 96.

⁶⁶ *Id.* at 152-58.

⁶⁷ This particular instance of airline competition has been recounted by Cherington, *supra* note 41, ch. VI; also see Stryker, *supra* note 65.

that did so, in 1948—spurred on, incidentally, by the success which the irregular operators were having. American did not enter the coach race until 1949 (but when it did so it used the DC-6 and offered coach flights at more convenient hours) and United remained on the sidelines until 1950. Once in the business American offered sharp competition, using the faster DC-7 for coach service in 1956 without any extra charge (United reluctantly followed suit in 1957).

Other instances of the value of having a number of competitors in the market can be cited. Capital (a small carrier, it should be noted) was the first to use turbocraft equipment (in 1955). National was the first to offer pure-jet service (in 1958). American inaugurated the family-fare plan. TWA offered the first mixed-class service (in 1955). Allegheny Airlines, a local-service carrier, provided the first no-reservation service. National, in 1959, initiated a service at less than coach rates, reflecting the sharp competition that has characterized the New York-Miami run since 1956.⁶⁸ And Eastern, on service between New York and Washington, began the since-highly successful air-shuttle, a no-reservation, no-waiting, less than coach fare service.

No one suggests that the foregoing illustrations add up to the unrestrained kinds of rivalry one might find in a market exhibiting a low level of concentration. But they are nonetheless of considerable value to the traveler. Without competition firms inevitably tend to be stodgy, lethargic, unduly skeptical of innovation; and this seems just as true, if not more so, where the industry is under government regulation. Eastern Air Lines, for instance, in the period before it was subjected to competition on its New York-Houston and St. Louis-Southeast routes, used old, poor equipment (even high-density coach-type seating configurations for first-class service) and generally offered a low grade of accommodation; indeed this was one major reason why the CAB authorized other lines to begin service over these routes.

But there is also value in having more than two carriers, *ceteris paribus*. Where there are only two competitors the probabilities are much greater that the tone of competition will be markedly less than if three are involved. In the latter case the impact each has on the other when inaugurating a given change in policy normally will be less pronounced, and thus more likely not to be followed—at least not promptly. Hence there is more incentive for experiment—with newer equipment, with a change in schedule, perhaps with a promotional fare arrangement (Eastern's use of the air-shuttle was adopted by Northeast Airlines, but only after several months had elapsed; and American has declined to follow at all—losing position in the market as a consequence).

The record strongly evidences the merits of competition in the industry and along specific routes. A larger number of competitors, even if it be

⁶⁸ National, Eastern, and Northeast have contested vigorously for traffic from the New York-New England area to Florida, offering significant fare concessions as an inducement. As of this spring seven different fares were in effect, depending on whether the trip was made at night or day, first class or coach, prop or jet; the fares ranged from a high of \$108.95 (one-way, without tax) to a low of \$58.65. Official Airline Guide (April 1962), pp. C-214/216, C-231, C-169/172. Of obvious benefit to the traveler, it is fair to conclude that this range of fare choices is the direct product of competition. On less competitive routes the range of choice is markedly less. In the face of such evidence it seems absurd to refer to useful rivalry of this type as "silly and truly noncompetitive," as did a writer recently, *New York Times*, Nov. 19, 1961, § 10, p. 1, col. 1-5.

only three instead of two, is likely to have distinct, though not always predictable, public reward. Implicitly the CAB appears to have shared this attitude in the period since 1955, for during this period it has greatly accentuated the degree of competition.

B. CAB Policy Since 1955

Let it be said at the outset that any effort to delineate CAB policy is fraught with danger, simply because the Board is noted for its propensity to alter its attitude frequently⁶⁹ and for its ability to obscure the grounds for its action. In the Board's behalf let it be admitted, however, that the pertinent statutory language is itself ambiguous. The Board is admonished by the Aviation Act to "consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity. . . . (d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce to the United States. . . ." This legislative declaration provides no clear guidance, in fact it is to a degree contradictory, and thus we should probably not be surprised at the Board's ambivalent interpretations.⁷⁰ From 1938 to about 1944, for example, it invoked "a strong, although not conclusive, presumption in favor of competition on any route which offered sufficient traffic to support competing services without unreasonable increase of total operating cost."⁷¹ Never did it articulate what amounted to "sufficient traffic" or what was an "unreasonable increase of total operating cost"; but still it seemed favorably disposed to more competition as a factor which assists in the fullest development of the national air transportation system.

Beginning about 1944, however, the Board abandoned the presumption doctrine. If existing service were deemed adequate new awards were rarely made, the Board majority (the dissenters usually referred to the decisions as reflecting an "anticompetitive philosophy") cynically disowning competition under such circumstances as amounting to no more than "competition for competition's sake"⁷² (reminiscent of language from the early depression years of the 1930's).

In 1955, under the guidance of its new chairman, Ross Rizley, the Board once more swung back to a policy of favoring competition wherever there was sufficient traffic.⁷³ Not only did it feel that competition was conducive to the vigorous development of air transportation, but it felt it might offer other advantages—such as eliminating airline subsidy by permitting weaker carriers to tap richer markets.

Commencing in 1955 the Board went about the job of increasing trunk airline competition with unrelenting zeal. In a series of decisions, begin-

⁶⁹ "The Civil Aeronautics Board in the course of its very short history has shown an almost incredible flexibility in moving toward and away from competition." Jaffe, Book Review, 65 Yale L.J. 1068, 1074 (1956).

⁷⁰ 72 Stat. 740 (1958), 49 U.S.C. § 1302 (1959).

⁷¹ Transcontinental and Western Air, Inc. et al., Additional North-South California Services, 4 C.A.B. 373, 375 (1943). The most comprehensive review of the Board's actions in this earlier period is Westwood, *Choice of the Air Carrier for New Air Transport Routes*, 16 Geo. Wash. L. Rev. 1 (1947), 16 Geo. Wash. L. Rev. 159 (1948).

⁷² E.g., Northwest Air, et al., Chicago-Milwaukee-New York Service, 6 C.A.B. 217, 228 (1944).

⁷³ For general treatments of the post-1955 period, see Richmond, *supra* note 64; Gellman, *The Regulation of Competition in the United States Domestic Air Transportation: A Judicial Survey and Analysis*, 24 J. Air L. & Com. 410 (1957), 25 J. Air L. & Com. 148 (1958); Richmond, *Creating Competition Among Airlines*, 24 J. Air L. & Com. 435 (1957).

ning with the *New York-Chicago Service* case in 1955⁷⁴ and most recently in the *Pacific-Southwest Local Service* case,⁷⁵ the CAB opened up a number of markets to other carriers, as indicated below:

SELECTED MARKETS WITH INCREASED COMPETITION, 1955-1961

Increased from one to two or more carriers

New York - Dallas	New York - Houston
Dallas - Los Angeles	Dallas - San Francisco
Chicago - Denver	St. Louis - Miami

Increased from two to three or more carriers

Los Angeles - San Francisco	New York - Miami
New York - Atlanta	New York - New Orleans
Chicago - Miami	

Increased from three to four or more carriers

New York - Detroit	New York - Chicago
New York - Washington	Boston - Washington

Between 1955 and 1957 the Board provided new or improved competitive service to at least 514 city pairs.⁷⁶ Dozens of routes which formerly had been the monopoly domains of grandfather carriers, particularly of the Big Four, were opened up to hunting by new entrants. The result was that where in 1955 more than 44% of revenue passenger miles were carried on routes effectively monopolized (i.e., where one carrier handled 90% or more of the traffic), by 1960 this had declined to 27.8%.⁷⁷

Unquestionably the Board has taken immense strides during the last seven years in increasing competition in the domestic trunk airline industry. What is less clear, however, is the precise rationale for its actions. Of course, it favored competition as a general rule; yet it also recognized that not all markets were suitable candidates because of inadequate traffic. But why it made the specific determinations in individual cases is not always clear. Indeed, as other critics have frequently pointed out (Louis Hector for one,⁷⁸ and more recently Judge Henry Friendly⁷⁹), the Board's opinions simply do not opine. Rather they recite any of a number of objectives that are deemed desirable, announce that the instant decision promises their fulfillment, and add the old caveat that the facts of each case govern. The result is to leave the reader with very little guidance for the future and with only a vague understanding of what explains the Board's conclusion.

Running through all of the major cases from 1955 to 1961 (and perhaps to date, although this is increasingly hard to determine), though, is the theme that "competitive service holds the greatest prospect for vigorous

⁷⁴ 22 C.A.B. 973 (1955).

⁷⁵ 1A Av. L. Rep. ¶ 21,248 (1962).

⁷⁶ Richmond, *supra* note 64, at 130 *passim*.

⁷⁷ Exhibits AE 153-54.

⁷⁸ Hector, *Problems of the CAB and the Independent Regulatory Commission*, 69 Yale L.J. 931 (1960). One of the reasons no doubt lies in the use of professional opinion writers. "Members of these opinion writing staffs explain that they consciously avoid statements of general principle as much as possible in the opinions they write, because they must be able to write an opinion justifying an opposite conclusion the next day, and hence must not be hampered by prior statements of general principles." *Id.* at 942-43.

⁷⁹ Friendly, *The Federal Administrative Agencies: The Need for Better Definition of Standards*, 75 Harv. L. Rev. 1055, 1072-97 (1962). Judge Friendly was formerly counsel to Pan American World Airways.

development of our national air transport system." This attitude appears to underly the various decisions, for once the Board takes this stance and repudiates the idea, as it did in the *Southwest-Northeast Service Case*,⁸⁰ that the existing service must be found inadequate before there can be any increase in route competition, conditions are manifestly conducive to additional service awards. This is not to say that the only goal which the Board has wished to achieve is an increase in competition. Indeed in every major case of the last seven years there were a number of factors involved in the decision. In some cases existing service was simply not adequate. On its New York-Houston⁸¹ and St. Louis-Miami operations,⁸² for instance, Eastern Air Lines, the only authorized carrier, had been using second-rate equipment and generally offering a low-grade service; competition, the Board felt, would provide a remedy, leading to more service and stimulating the established carrier as well.

But in the final analysis the CAB has been governed by the feeling that competition is desirable per se and offers a way to achieve greater balance in the industry without working significant economic hardship on the bigger carriers. In the *New York-Florida Case*,⁸³ for instance, the Board authorized Northeast Airlines to provide a third-carrier service between points in the northeast and Florida. One of the principal reasons for doing so, and in preferring Northeast over other applicants (Delta most notably), was to give Northeast access to a high-density, long-haul market in the expectation that this would make continued subsidy unnecessary. In the *Southwest-Northeast Service Case* the Board, in awarding Braniff the New York-Dallas route, explained:

Unless the relative economic opportunity — and basically this means route systems — of the smaller carriers approaches more closely that of the Big Four, their competitive position and ability to weather economic adversity are bound to suffer. . . . It is of considerable significance that the dominance of the Big Four flows from their access to the high-density markets, and this enables them to attain greater economy in operating costs and flexibility in scheduling of service.⁸⁴

This policy also largely explains route awards to Capital and Northwest in the *New York-Chicago Service Case*⁸⁵ and to National in last year's *Southern Transcontinental* decision.⁸⁶

In making the various competitive awards the Board has been obligated, of course, to consider the scale of the respective market in assessing whether the existing carrier(s) can withstand competition. In the *New York-Chicago* case, as an illustration, American Airlines argued that the

⁸⁰ *Southwest-Northeast Service Case*, 22 C.A.B. 52 (1955).

⁸¹ *Id.* at 65.

⁸² "There is considerable evidence in the record to show that the service provided by Eastern is not comparable with that offered in competitive markets. . . . For example, the record shows that Eastern continued to use five-abreast seating in first-class flights until late 1956, long after it had introduced more convenient configuration in competitive markets; and the carrier utilized only slow unpressurized DC-4 aircraft for St. Louis-Miami nonstop service until the winter of 1956. In addition Eastern failed to provide nonstop service with modern equipment between St. Louis and Atlanta until 1956. At most, Eastern provided only limited frequencies in the St. Louis-Southeast markets, with resulting space shortages and unduly high load factors." *St. Louis-Southeast Service Case*, 27 C.A.B. 342, 346 (1958).

⁸³ 24 C.A.B. 94 (1956).

⁸⁴ 22 C.A.B. 52, 57-58 (1955).

⁸⁵ 22 C.A.B. 973 (1955).

⁸⁶ 1A Av. L. Rep. § 21,131 (1961).

New York-Detroit route could not support more than a single carrier. To this contention, a kind that can be found in each major decision, the Board replied, in rather typically evasive fashion:

In our judgment, the size and potential of the New York-Detroit market will now support three turnaround services rather than merely one heretofore operated by American. Thus the record shows that in this area the New York-Detroit market is exceeded only by the New York-Chicago market, and yet American is the only unrestricted operator between New York and Detroit. The much smaller New York-Cleveland market has two turnaround services. Furthermore, the New York-Detroit market increased by 86 percent from 1949 to 1954. Under such circumstances, we have no hesitation in finding that the New York-Detroit market will support two additional services.⁸⁷

This is really no more than a bootstraps argument, for one can search without avail for an explanation of why the New York-Cleveland market can support two services. Moreover, even if the Cleveland route can sustain two rivals, what rationalizes three in the Detroit market (why not just two, or perhaps four)? The other decisions are likewise unhelpful. Thus, a third service was authorized between New York and Miami with the bare explanation that "there can be little question that the markets here involved are in material aspects more than comparable to those for which in recent cases we have authorized service by more than two carriers";⁸⁸ between the Great Lakes and the South ("We are convinced that the traffic is sufficiently large now and has the inherent potential to support another carrier in addition to Delta and Eastern. The Chicago-Miami market is by far the largest two-carrier market in the country and has shown an impressive continuing growth. . . .");⁸⁹ and just this year between Los Angeles and San Francisco (this "is one of the largest air traffic markets in the country . . . the tremendous traffic generating ability of the market accounted for more than a million local passengers in 1958, even outproducing the important New York-Miami market").⁹⁰ Similar language, equally unsatisfying, can be found in other opinions supporting awards which meant a competing (or second) carrier, as in the *St. Louis-Southeast Service Case*⁹¹ and in the *Southwest-Northeast*⁹² decision.

While it is not always easy to detect the logic in the Board's decisions, the fact clearly is that from 1955 to 1960 the extent of airline competition in the United States was greatly expanded. As mentioned earlier, the monopolized routes declined from 44% to 27.8% during those five years. Moreover, the amount of traffic carried on routes where only two airlines competed also declined as a result of additional awards; from 1955 to 1960 the proportion of revenue passenger miles carried on routes where there were three or more effective competitors rose from 15.8% to 32.4%. But this does not reveal the extent to which the various trunk airlines individually were affected. Table 6 presents this information.

⁸⁷ 22 C.A.B. 973, 991 (1955).

⁸⁸ 24 C.A.B. 94, 98-99 (1956).

⁸⁹ Great Lakes-Southeast Service Case, 27 C.A.B. 829, 846 (1958).

⁹⁰ Pacific-Southwest Local Service Case, 1A Av. L. Rep. ¶ 21,248 (1962), at pp. 14,715-16.

⁹¹ St. Louis-Southeast Service Case, 27 C.A.B. 342 (1958).

⁹² 22 C.A.B. 52 (1955).

TABLE 6. AMOUNT OF TRAFFIC CARRIED BY DOMESTIC TRUNK AIRLINES UNDER MONOPOLY AND COMPETITIVE CONDITIONS
(percentage of revenue passenger miles carried)

Carrier	Monopoly Traffic		Traffic on Routes with Two or More Other Carriers	
	1955	1960	1955	1960
American	41.4%	22.8%	30.7%	39.1%
Braniff	67.6	49.8	0.3	5.1
Capital	50.8	29.5	9.9	26.4
Continental	87.5	34.8	0.1	27.4
Delta	62.1	41.1	0.8	18.6
Eastern	53.7	26.3	1.6	31.4
National	19.8	22.0	1.0	55.4
Northeast	91.3	20.1	8.4	66.8
Northwest	40.7	26.1	0.2	13.2
TWA	37.1	21.2	25.2	42.9
United	38.7	29.0	19.3	29.5
Western	45.6	46.6	7.9	9.9
Weighted average	44.4	27.8	15.8	32.8

Source: Exhibits AE 153-54.

As is evident, by 1960 all but two of the airlines carried less traffic under monopoly conditions than in 1955. But the smaller carriers received most of the new route awards, thus tending to offset the greater degree of competition they were being subjected to in their older markets. In terms of new service authorization equivalent to or better than that of the least restricted other carriers, Professor Richmond found that 88% of the new passenger exposure and 83% of the passenger mile exposure went to the smaller eight (now seven) airlines. American and Eastern received access to less than 1% of the potential new passenger miles. United gained access to about 4%, and, surprisingly, TWA about 13% (this was as good as for any other carrier except Northeast).⁹³ On paper, therefore, the smaller carriers received the bulk of the new route awards, after making adjustment for operating restrictions and other such factors. But what are the lessons of history? How have the various carriers been affected?

C. General Consequences

In spite of the CAB's strong efforts to achieve greater balance within the industry by granting the smaller airlines access to richer routes, the Big Four still retain a commanding position within the industry. In 1955, the last year before the Board's new policy took hold, the four leading airlines carried about 74.5% of all revenue passenger miles. By 1960, as Table 7 shows, this share had declined, but only slightly, to 71.5%; in 1960 it rose to 73.0% (largely because of the United-Capital merger). The share of revenue mileage held by the smaller carriers increased in every case except for the Northwest and National (whose position will definitely improve due to its 1961 *Southern Transcontinental* award).⁹⁴

⁹³ Richmond, *supra* note 64, ch. IX and especially tables IX-5/IX-14.

⁹⁴ *Supra* note 86.

TABLE 7. REVENUE PASSENGER MILES FLOWN, TRUNK AIRLINES, 1953-1961

Carrier	1961	1960	1959	1958	1957	1956	1955	1954	1953
American	5,965	6,257	5,614	4,891	5,036	4,793	4,266	3,372	3,210
% of Total	20.1	22.2	20.0	20.0	20.6	22.2	22.3	20.9	22.7
United	7,496	5,355	4,827	4,915	4,583	4,249	3,754	3,135	2,575
% of Total	25.0	19.0	17.2	20.1	18.7	19.7	19.7	19.4	18.2
Eastern	4,007	4,046	4,432	3,811	4,397	3,788	3,342	2,847	2,309
% of Total	13.5	14.4	15.8	15.6	17.9	17.5	17.5	17.6	16.3
TWA	4,287	4,451	4,579	3,662	3,656	3,261	2,866	2,611	2,370
% of Total	14.4	15.8	16.3	15.0	14.9	15.1	15.0	16.2	16.8
Big 4 Total	21,755	20,109	19,452	17,279	17,672	16,091	14,228	11,965	10,464
Big 4 % of Total	73.0	71.5	69.2	70.7	72.1	74.5	74.5	74.1	74.0
Braniff	1,070	1,053	935	913	865	718	605	537	463
% of Total	3.6	3.7	3.3	3.7	3.5	3.3	3.2	3.3	3.3
Capital	*	1,492	1,611	1,413	1,513	1,019	792	746	695
% of Total		5.3	5.7	5.8	6.2	4.7	4.1	4.6	4.9
Continental	902	885	672	419	363	259	221	167	148
% of Total	3.0	3.1	2.4	1.7	1.5	1.2	1.2	1.8	1.1
Delta	2,189	1,832	1,556	1,400	1,314	1,124	953	787	624
% of Total	7.4	6.5	5.5	5.7	5.4	5.2	5.0	4.9	4.4
National	1,137	1,016	1,101	990	894	945	850	694	572
% of Total	3.8	3.6	3.9	4.1	3.6	4.4	4.4	4.3	4.0
Northeast	752	565	519	407	245	119	116	104	91
% of Total	2.5	2.0	1.8	1.7	1.0	0.6	0.6	0.6	0.6
Northwest	1,025	1,337	1,384	1,111	946	872	823	749	720
% of Total	3.5	4.8	4.9	4.5	3.9	4.0	4.3	4.6	5.1
Western	874	944	896	503	687	457	514	401	359
% of Total	2.9	3.4	3.2	2.1	2.8	2.1	2.7	2.5	2.5
TOTAL	29,704	28,126	28,126	24,435	24,499	21,604	19,102	16,150	14,136

* Capital's mileage, 601 million for the first five months of 1961 is included in that of United due to their merger. For earlier years the effects of other mergers involving the trunk airlines listed is similarly treated.

Source: Civil Aeronautics Board.

Northeast (because of its 1956 New York-Florida award), Continental (with recent extensions from Chicago to Denver and Denver to Los Angeles), and Delta (benefitting from service authorizations between New York and Houston, New Orleans, and Atlanta) registered particularly healthy traffic increases.

In the final analysis, however, what counts is profits. As the foregoing discussion and the details presented in Table 7 demonstrate, the smaller carriers generally gained some traffic at the expense of the larger airlines, particularly American and Eastern. But the recently-authorized awards have not bolstered profitability for the weaker carriers in spite of their heavier passenger traffic. Northeast is not a good test (it was in serious difficulty when it was granted entry to the New York-Miami market),⁹⁵ but even Delta and Continental, which, relatively, benefitted more than the other lines, still found their profit margins slipping between 1955 and 1961. The same is true for all of the others. One is properly entitled to ask: what happened?

For one important thing passenger traffic has not increased as rapidly since 1957 (precisely when the CAB began to make its numerous new competitive route awards) as in the immediately preceding years. Take the New York-Washington route as an illustration. In 1956 this route was dominated by American and Eastern, the former carrying some 63% of the passengers who moved between those two points. Northeast Airlines was thereupon authorized to serve the route, the Board insisting that whatever diversion would result will "come out of future traffic growth in the markets involved."⁹⁶ But by 1961, as Table 8 shows, traffic between the two points had increased by only about 10% (or about half that of the domestic trunk industry as a whole). Of this somewhat larger market American now carried 26% of the total, Eastern 42%, and Northeast about 20% (the remainder divided among National and other carriers). Thus, while the market had expanded, it had not done so sufficiently to offset the dilution that Northeast's entry had brought about. The same is true of the most important of the other routes over which increased competition had been sanctioned. Indeed, just as the Board began to step up the degree of competition, relying on the markets' rapid past growth, traffic dried up, as Table 8 well demonstrates. The New York-Miami route, where traffic had increased by 51% from 1954 to 1957, grew by only 3.6% from 1957 to 1960. The New York-Houston and New York-New Orleans markets actually shrunk. Hence the various pies which the Board decided to carve into a larger number of pieces, on the theory that the pies would get bigger and continue to be divisible equitably, simply stopped growing—with rare exception. What is responsible for this sharp decline in the rate of passenger traffic growth is not easily determined. No doubt the two recessions, 1957-1958 and 1960-1961, bear some of the blame. A miscellany of other explanations could be added. But, as the discussion earlier suggested, the rapid post-1958 fare increases cannot be overlooked. While airline fares had not increased at all between 1954 and 1957, from 1957 to 1960 fares went up by about 21% (if the jet differ-

⁹⁵ Indeed at the time the award was made two members of the Board dissented, with Member Denny firmly convinced that Northeast was simply not able to make effective use of the Florida routes. For one thing it lacked equipment comparable in size and speed to that already in use by Eastern and National. 24 C.A.B. 94, 124 (1956).

⁹⁶ 24 C.A.B. 94, 105 (1956).

ential is taken into account). It is reasonable to expect that this would have a particularly noticeable impact on routes heavily patronized by tourists, such as New York-Miami or New York-New Orleans. Obviously other forces have been at work; but it is foolish to think that fares can be raised without retarding traffic growth.

TABLE 8. AIRLINE TRAFFIC GROWTH, SELECTED MARKETS, 1954-1960

Market*	Year (millions of revenue passenger miles flown)			Percentage Increase	
	1954	1957	1960	1954-1957	1957-1960
Total, All Trunk Traffic	16.20†	24.4†	29.2†	51%	21%
New York - Detroit	111	163	182	47	12
New York - Chicago	393	514	596	31	16
New York - Miami	651	984	1,019	51	4
New York - Dallas	80	127	168	59	32
New York - Washington	101	135	149	34	10
New York - Boston	101	139	167	38	20
New York - Houston	87	129	124	48	-4
New York - New Orleans	67	110	97	64	-12
New York - Atlanta	64	84	95	31	13
Chicago - Denver	31	47	66	52	40
Chicago - Detroit	52	63	64	21	2
Denver - Los Angeles	35	65	100	86	54
Chicago - Los Angeles	255	349	478	37	37
New York - San Francisco	444	663	780	49	18
New York - Cleveland	77	111	118	44	6

* Markets selected are ones in which degree of competition has been covered by CAB action, 1955-1962.

† In billions

Source: CAB. Competition Among Domestic Air Carriers; Richmond, *supra*, note 64, appendix 3; 1962 ATA Facts and Figures, p. 17

Since it possesses the power to suspend fare proposals made by the airlines the CAB may, therefore, actually have been working at cross-purposes over the past seven years—accepting substantial fare hikes that were likely to slacken the very traffic growth that was essential to the successful implementation of its policy of increasing competition. There are some indications that the Board may recognize this possible inconsistency. Recently it has spoken clearly of the need for greater promotional efforts on the part of the airlines. In 1960 it approved a low-cost "air-bus" service between Pittsburgh and Miami, saying that this was consistent with its policy of "encouraging the filing of fares designed to promote air travel, particularly the low fare type of service designed to enable air transportation to penetrate more effectively into a larger market."⁹⁷ Nevertheless the Board insists that all air fares cover fully all allocated costs. (It reflected this attitude a few months ago in the *Pittsburgh-Philadelphia No-Reservation Fare Investigation*.)⁹⁸ This means that the airlines have too little room in which to experiment with fare reductions,

⁹⁷ Eastern Air Lines, Inc.—In the Matter of Local "Air-Bus" Passenger Fares, 1A Av. L. Rep. ¶ 21,067 (1960).

⁹⁸ 1A Av. L. Rep. ¶ 21,230 (1961).

strongly reinforcing their customary propensity to price in a highly conservative fashion. One is definitely reminded of the practice of the electric utilities to wait for consumption to increase before reducing prices; the airlines, too, believe that the demand for their services is inelastic until they see conclusive evidence to the contrary—in response either to fare increases or reductions. At the moment the trend to higher fares is clearly evident, with the airlines proposing and the CAB usually approving (with occasional minor modifications). This is well calculated to inhibit traffic growth and accentuate the problems created by the various competitive awards which have been made in recent years.

To American Airlines and the other advocates of trunkline mergers, however, the recent decline in carrier profits is explained basically by just one thing: increased competition stemming from the CAB post-1955 route awards. They find a distinct correlation between the decline in the amount of traffic carried under monopoly conditions and the shrinkage in airline profits.⁹⁹ In their opinion the immediate answer lies in a lessening of competition, and this they insist can best be accomplished through consolidation. There are, however, several flaws in this line of argument. First, if Northeast Airlines, which has been in serious difficulty since long before the CAB embarked on its program of stepping up competition in 1955, is excluded from the analysis, along with National, any meaningful mathematical correlation between profitability and the amount of monopoly traffic collapses.¹⁰⁰ Second, the recent decline in airline profits is at least as well explained by a reduction in the rate of growth of passenger traffic and by other factors, ranging from recession to the costs of jet acquisitions and their introduction, as by the Board's policy of increasing competition since 1955. The latter, of course, has contributed to airline problems, but it is not their cause. Third, explicit in the American-Eastern argument is the idea that increased competition accelerates costs and that, if curtailed, expenses could be reduced sufficiently to yield reasonable returns. For the trunk airlines as a group the cost per available ton mile went up from 26¢ to 29¢ between 1955 and 1960, and per revenue ton mile from 46.1¢ to 57.2¢. American insists that these increased expenses are attributable predominantly to increased competition and that if competition could be cut back to its 1955 level aggregate airline costs would fall by \$200 million. But there are at least two difficulties with this presentation. For one, while costs have increased since 1955, so too have revenues; thus revenue per revenue ton mile has increased over this period from 51.6¢ to 58.3¢, more, relatively, than the cost per available ton mile.¹⁰¹ The fact that the cost per revenue ton mile went up more than revenue per revenue ton mile suggests that the amount of service offered was unwisely expanded; it is difficult to link this with competition per se. Moreover, as a general matter the proof offered by American Airlines fails to establish that rising costs are attributable solely or even largely to more intensive competition. Rather they seem more easily traceable to the expenses incurred for jet purchases and introduction, to special conditions

⁹⁹ The American Airlines evidence is contained in a number of statistical exhibits. See exhibits AE-151/155, as explained in AE-F.

¹⁰⁰ Exhibit NAL-500/501. National and Northeast are the boundary specimens; in 1955 the former was the most profitable carrier although it had the least amount of monopoly traffic, and Northeast was the least profitable although it had the greatest amount of monopoly traffic.

¹⁰¹ Exhibit AE-F, p. 4. For a rebuttal see NAL-500/501.

(equipment modifications, for example), and to a sharp drop in the growth of passenger traffic. Relevant to the latter is the information that Continental Airlines reported a drop in its costs per revenue ton mile from 1955 to 1960 as the apparent result of an increase in its passenger traffic. Suffice it to say that under these circumstances to blame competition for the recent decline in industry profits is totally unwarranted. Fourth, to the extent that a curtailment in existing levels of competition might be in order (as where independent study by the CAB might determine competition to be improvident beneath a certain traffic level), there is still grave doubt that airline consolidation represents the best means of accomplishing this objective.

The question of mergers, though, deserves further analysis, for it is the contention of American Airlines that merger, specifically with Eastern Air Lines, not only represents a solution to airline financial problems (an unconvincing argument, as indicated above), but will provide substantial public benefit without significant detriment. If this is true, then airline mergers may be desirable, whether they are proximately related to the industry's economic difficulties or not. Accordingly the American-Eastern merger, as a prime case in point, deserves close inspection—within a broader framework of the CAB policy as to mergers and their competitive implications.

III. MONOPOLY, COMPETITION AND THE AMERICAN-EASTERN MERGER

American Airline's application for approval of its merger with Eastern Air Lines, a consolidation viewed by the petitioners as the solution to their problems and as a guide for the remainder of the industry, is now pending before the CAB. At this writing the hearing has just been finished, one that summoned forth the active intervention of most of the other trunk airlines (with Delta being particularly active in opposition) as well as diverse other organizations, not to overlook the Department of Justice.¹⁰² It is American Airlines, however, which has the obligation in effect of going forward and establishing that the merger "will not be inconsistent with the public interest" and will not result "in creating a monopoly or monopolies."

In its behalf American argues principally that the merger will curtail some of the competition that has been generated of late by improvident CAB awards. (Admittedly this amounts to a slap in the face, but it is what the argument amounts to, devoid of diplomatic language.) Moreover, it is contended, the affiliation with Eastern provides an opportunity for achieving greater operating efficiency and permits new, through service connecting a number of the country's cities. American and Eastern now serve thirty common locations; in itself this means they can combine ticket offices, airport terminal facilities, hangars, etc. As well, since American's peak travel season occurs in the summer while Eastern's is in the winter, their capital requirements can be significantly reduced and more intensive use made of existing flight equipment. Thus the merger promises greater efficiency, lower costs, and improved service. As sort of a bonus, all of these qualities can be accomplished without adverse competitive effect. If so, it is indeed a rare and attractive undertaking. But

¹⁰² Nor the CAB's own Bureau of Economic Regulation, which has opposed the merger.

there is reason to doubt the validity of these representations, particularly as to the merger's competitive consequences. To put this aspect of the case in its proper setting, however, first requires a perusal of the relevant legislation and of the Board's past merger decisions.

A. Mergers And The CAB: A Search For Standards

All mergers between airlines must be authorized by the CAB before they can be lawfully consummated¹⁰³—but section 408(b) of the Federal Aviation Act of 1958 (in this respect identical to the comparable provision in the original 1938 federal legislation) requires approval unless the Board finds that the proposed arrangement “will not be consistent with the public interest.”¹⁰⁴ This provision represents one of the principal ways in which the issue of competition-versus-monopoly is presented, for in defining “public interest” the Board invariably turns to section 102 of the Act which declares, as being in the public interest, “competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States. . . .”¹⁰⁵ Although this statutory declaration is lacking in any desirable degree of precision, nevertheless in its past consideration of merger applications the Board has leaned heavily on its language in finding that a given proposal was not consistent with the public interest. This was true in two of the leading merger cases, one involving United's proposed acquisition of Western Air Lines,¹⁰⁶ and the other American's planned purchase of Mid-Continent Air Lines.¹⁰⁷ In both decisions the Board seemed primarily disturbed over the possibility that the contemplated mergers, in each instance involving one of the Big Four and a markedly smaller truck carrier, would accentuate the overall degree of industrial concentration, contribute to greater imbalance and injure the weaker airlines. In the former United, operating from New York to San Francisco, and also authorized to fly between Seattle and San Diego, proposed to acquire Western, a major north-south system in the Pacific coast region. The two lines intersected at Salt Lake City. As the Board viewed the facts the merger would give United direct access to the entire west coast area for the origination of transcontinental traffic. This, it felt, was undesirable. “To allow one air carrier to obtain control of air transportation in the West Coast area greatly in excess of that possessed by competitors would . . . seriously endanger the development of a properly

¹⁰³ 72 Stat. 767 (1958), 49 U.S.C. § 1378(a) (1959). Once the Board approves a merger the parties affected are “relieved from the operations of the ‘antitrust laws’.” 72 Stat. 770 (1958), 49 U.S.C. § 414 (1959).

¹⁰⁴ 49 U.S.C. § 1378(a) (1959).

¹⁰⁵ 72 Stat. 740 (1958), 49 U.S.C. § 1302 (1959). In considering a similar legislative declaration pertaining to mergers coming under the jurisdiction of the Interstate Commerce Commission, the Supreme Court has ruled that the “public interest” criterion requires the ICC to “consider the effect of the merger on competitors and on the general competitive situation in the industry in the light of the objectives of the national transportation policy.” The Court rejected the argument that the agency might disregard the antitrust policy since the statute did not expressly require its application. “Congress . . . neither has made the anti-trust laws wholly inapplicable to the transportation industry nor has authorized the Commission in passing on a proposed merger to ignore their policy.” *McLean Trucking Co. v. United States*, 321 U.S. 67, 86-87 (1944).

¹⁰⁶ *United Air Lines Transport Corporation—Acquisition of Western Air Express Corporation*, 1 C.A.A. 739 (1940).

¹⁰⁷ *American Airlines, Inc., Acquisition of Control of Mid-Continent Airlines, Inc.*, 7 C.A.B. 365 (1946).

balanced air-transportation system in this region."¹⁰⁸ A similar philosophy was apparent in the disapproval of American's purchase of Mid-Continent, the latter operating north-south, bisecting the nation in a relatively narrow path running from Minneapolis-St. Paul through Kansas City and Tulsa to New Orleans and Houston, with two legs extending into St. Louis. The Board, noting also that the two systems were relatively uncomplementary, was largely influenced by the possibility that American would have an undue competitive advantage in obtaining business, originating to and destined from points on the Mid-Continent routes. "[T]he wider the geographical scope of a carrier's operations in comparison with a particular rival, the greater the competitive advantage which it will enjoy through the control of traffic originating at or destined to points to which the other carrier does not have access."¹⁰⁹ (The close relevance of this statement to the American-Eastern merger can be noted later.)

The statute, while on the one hand requiring the approval of airline mergers unless found inconsistent with the public interest, also provides that "the Board shall not approve any consolidation . . . which would result in creating a monopoly or monopolies and thereby restrain competition or jeopardize another air carrier not a party to the consolidation. . . ."¹¹⁰ Strangely, this part of the statute has received little clarifying interpretation. The Board, in disapproving a merger because of its competitive implications, has chosen over the years to rest its decisions, not on the monopoly proviso, but rather on the looser formulation of inconsistency with the public interest. Indeed, so far the CAB has not faced squarely the problem of implementing the monopoly proviso at all. Now the American-Eastern merger presents this precise issue and the Board can responsibly avoid the problem no longer.

The closest the CAB has come to defining the term "monopoly," as used in the Act, was in the 1940 *United-Western Interchange* ruling. There it determined, first of all, that "restraint of competition" is a factor "only if it results from that degree of control which [it] decides constitutes a monopoly of air transportation."¹¹¹ Thus, if there is no monopoly, there can be no restraint of competition, or at least so the Board interprets the Federal Aviation Act. Thus the ultimate test is whether the merger will result in creating a "monopoly." How then is that term to be defined? The Board, through a rather remarkable use of near meaningless words, has so far avoided any intelligent response.

In *United-Western*, the first and what in many respects remains the clearest case on the point, the Board said that "the word 'monopoly' . . . refers to a particular degree of control of air transportation, or any phase thereof, in any territory or section of the country." The "particular degree of control," of which the Board speaks, is said to refer to "the control of a particular business or article of trade, without regard to the results which may flow therefrom."¹¹² This is hardly satisfying. And in attempting to apply this definition the Board has only made the matter more obscure. For example, in approving a merger between Braniff and

¹⁰⁸ *Supra* note 106, at 750.

¹⁰⁹ *Supra* note 107, at 378.

¹¹⁰ 49 U.S.C. § 1378(b) (1959).

¹¹¹ 1 C.A.A. 723, 733-34 (1940).

¹¹² *Ibid.*

Mid-Continent the Board noted that these two carriers had provided the only direct service between Kansas City and Houston. Certainly this would seem to create a monopoly of service between the two points, what could readily be termed a section of the country. But the hearing examiner (affirmed by the Board) concluded otherwise, saying that

this removal of competition for passengers traveling between . . . [these two points] will not affect the amount of service now available, but on the contrary it appears that additional services will result. . . . Accordingly, it appears that the substitution of the merged company for the two separate companies, insofar as the provision of service between Kansas City and Houston is concerned, will not result in creating a monopoly which will restrain competition or jeopardize air carriers not a party to the merger.¹¹³

What this seems to mean is that while a monopoly admittedly was created, it was not such as to restrain competition. If this is an accurate reading, it makes no sense: the essence of monopoly is restraint of competition, for if the latter were not achieved indeed there could be no monopoly. It may, on the other hand, amount to a conclusion that no monopoly was created, even though the merger involved the only two airlines providing the only service between given locations. This likewise makes little sense.

Perhaps what the Board has in mind, without clearly saying so, is the notion that if a merger holds out the promise of better service (or more efficient operations, or what have you), the fact that it eliminates a competitor is unimportant.¹¹⁴ This, if true, is implausible for if airlines *A* and *B*, which provide the only service between two given locations or which provide the bulk of the service (say, $\frac{2}{3}$ or more), merge, it is difficult to argue that no monopoly has been established.¹¹⁵ And the statute, whether one agrees or not, enjoins the Board from approving any merger the effect of which is to create a "monopoly or monopolies"; the fact that better service might result is completely beside the point. In this respect Congress clearly favored competition to monopoly, come what may.

Even though the CAB's handling of the competition-monopoly problem leaves a good deal to be desired, the standards which it has set forth, as outlined above, provide a general framework within which to appraise the merits of the American-Eastern merger. It will be useful to recall,

¹¹³ Braniff-Mid-Continent Merger Case, 15 C.A.B. 708, 735 (1952).

¹¹⁴ See Acquisition of Marquette by TWA, 2 C.A.B. 1 (1940). In upholding the Board's approval of last year's United-Capital merger the Court of Appeals for the District of Columbia, in a rather casual discussion of the issues, took something of the same attitude. It concluded that the consolidation would not create a monopoly, looking at the "whole picture" (whatever that means). Admitting that on four specific routes a monopoly would result the Court nevertheless said the merger would create competition, substituting a stronger carrier for a weaker. Northwest Airlines, Inc. v. CAB, 2 Av. L. Rep. 17,809 (D.C. Cir. 1962).

¹¹⁵ At an early date the CAA seemed to recognize the necessity of defining the relevant market in assessing the likelihood that a monopoly would be created. United Air Lines Transport Corporation and Western Air Express Corporation—Interchange of Equipment, 1 C.A.A. 723 (1940). There the agency said that the term "monopoly" refers to "a particular degree of control of air transportation, or any phase thereof, in any territory or section of the country," citing authority which directly involved the matter of market definition. *Id.* at 733-34. And within the context of air transportation it is perfectly reasonable to argue that the "market" consists of the direct routing between certain cities. Hence, where a merger will join, say, the only two carriers operating on a given route, monopoly is the result and the statute forbids the approval of mergers in such cases. Furthermore, less than total control of a given market can also amount to monopoly, as the courts have pointed out in their interpretation of section 2 of the Sherman Act. At least with two-thirds of the market—probably much less—a firm can exercise a high degree of control over price and other relevant variables, and this control is the ultimate criterion of monopoly. See *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945).

too, that since 1955 the Board has been intent on creating additional competition on the routes served by the trunkline industry. Really, therefore, two kinds of policy considerations are in issue: (1) the declaration of the Aviation Act permitting approval of mergers only if not inconsistent with the public interest and unless productive of monopoly; (2) the Board's post-1955 policy of increasing route competition as a means of achieving greater balance within the industry and insuring maximum development of the domestic air transport system.

B. The American-Eastern Merger

The merger of Eastern Air Lines into American Airlines, agreed to by their respective boards of directors on January 23, 1962, would create a massive corporate entity, with assets of \$950 million—greater than those of RCA or General Dynamics, or of such large railroads as the Chesapeake & Ohio and the Baltimore & Ohio. Within the airline industry itself a combined American-Eastern would become the largest carrier, regardless of the standard of comparison. In 1961 American accounted for 20% of all revenue passenger miles flown by the trunk airlines in domestic operations, Eastern for 13.5%. Together, therefore, they would represent a third of the total passenger traffic. In conjunction with last year's United-Capital merger (which made United the nation's biggest one airline), amalgamation of American and Eastern means that the two biggest airlines together would dominate about 60% of trunk airline traffic and that the three largest (including TWA) would account for about 75%. The result clearly would be a sizeable increase in the level of concentration, far more than offsetting in one step all of the Board's efforts over the last several years to achieve less concentration and greater industrial balance. Moreover, the likely effect of the proposed merger would be to trigger off a series of other consolidations, as the surviving carriers struggled (rationally or otherwise) to maintain relative position within the industry. Certainly if the Board swallows this proposed merger it will have immense difficulty in rejecting a number of other consolidations, most of which would involve aggregations of capital and passenger traffic of far less magnitude. Interestingly, it is precisely these kinds of considerations that led Judge Weinfeld to forbid a merger of Bethlehem Steel and Youngstown Sheet and Tube in 1958.¹¹⁶ There the parties together possessed about 21% of total steel ingot capacity; merger promised to entrench Bethlehem in number two place in the industry and also to lead to further concentration, giving the top two firms nearly 50% of ingot capacity; as well, if this merger were tolerated, he reasoned, it would be likely to inspire other mergers to which it would be difficult to object. While the Bethlehem-Youngstown case was brought under section 7 of the Clayton Act, the kinds of competitive repercussions it was thought to present are directly relevant in evaluating the American-Eastern proposal.¹¹⁷

¹¹⁶ *United States v. Bethlehem Steel Corporation*, 168 F. Supp. 576 (S.D.N.Y. 1958). And precisely these kinds of factors were also involved in the recent *Brown Shoe* decision, where the Supreme Court upheld a section 7 violation. *Brown Shoe Co. v. U.S.*, 370 U.S. 294 (1962).

¹¹⁷ Moreover, the CAB is charged with the responsibility of enforcing section 7 of the Clayton Act in respect to mergers within its jurisdiction. 15 U.S.C. § 21. Even though the effect of the Board's approval is to exempt the parties to a merger from the "antitrust laws,"

Laying aside the effect of the American-Eastern merger on overall industry concentration, the impact on routes where the two airlines are now in direct competition must be assessed. As a very general matter American operates from the northeastern part of the country (including such major points as New York, Boston, and Washington) southwest through Chicago, Cincinnati, and St. Louis to Dallas and the West Coast. Eastern operates mostly in a north-south direction, reaching Miami, Atlanta, New Orleans, and Houston from such northern points as New York, Pittsburgh, Detroit, Chicago, and St. Louis. Many of Eastern's routes are concentrated in the southeastern quadrant, blanketing the Carolinas, Georgia, Alabama, and Florida. Viewed in this manner merger between the two companies seems to threaten no loss in competition. But a closer look at the routes indicates several areas where they are in direct competition.

Most of their face-to-face competition comes in the northeastern area, between such cities as Boston, Providence, Hartford, New York, Philadelphia, and Washington. But the two also compete in service between points in that section and others in the central United States—such as New York-Louisville and Boston-St. Louis—and within the central region itself—such as Chicago-Indianapolis and Chicago-Cincinnati.

Table 9 arrays a number of the routes where the two airlines now compete beginning with those where they provide the only service (Houston-Cleveland); or virtually all of it (New York-Louisville), to those where they meet substantial competition from other airlines (Boston-Washington). As is evident, on at least a dozen routes American and Eastern provide the only competition; over another five American and Eastern together carry 90% or more of the passenger traffic.¹¹⁸ Obviously in these cases merger will mean the elimination of all effective competition. While these routes vary greatly in the amount of traffic generated, as indicated in Table 9, it cannot be denied that acceptance of this merger means the acceptance of monopoly where competition (albeit duopolistic) now reigns.

Even over routes where American and Eastern presently encounter significant competition from other carriers, as between New York and Washington, they nevertheless frequently account for the biggest chunk of the traffic. While one frequently sees references to the large number of carriers authorized to serve various of the northeast routes, the fact remains that as to several of them American and Eastern are nevertheless dominant—as in the case of New York-Boston, New York-Washington, New York-Hartford, and Baltimore-New York. Here merger will mean not only conferring on one carrier an effective monopoly, but, perhaps even more important, the elimination of a substantial independent competitor from the market. The significance of this seems particularly striking insofar as service along the upper eastern seaboard is concerned, for it is here where, within only the last year, Eastern has shown particular imagination with its inauguration of an air-shuttle service. While it is

there remains a serious question whether the Board can disregard section 7 in reaching its decision. If it cannot, then section 7, which represents a greater hurdle than the monopoly proviso, must also be satisfied before any merger can be authorized. So far the issue has not been satisfactorily resolved.

¹¹⁸ A more comprehensive listing of routes on which American and Eastern now compete is contained in exhibit BER-10. Exhibit AE-601 presents similar information.

TABLE 9. DIVISION OF PASSENGER TRAFFIC IN SELECTED MARKETS WHERE AMERICAN AND EASTERN COMPETE

Market	Total Revenue Passenger Miles in Millions, 1960*	Percentage of Traffic Carried by†		
		American	Eastern	Other
Houston-Cleveland	6.5	71	29	
Louisville-Nashville	2.3	47	53	
San Antonio-Hartford	3.5	33‡	67‡	
Syracuse-Baltimore	0.8	35	65	
Syracuse-Louisville	0.8	47	53	
San Antonio-Philadelphia	9.5	31	69	
San Antonio-Providence	1.2	40	60	
Charleston-Chicago	3.2	50	46	4
New York-Louisville	40.0	32	63	5
Charleston, W. Va.-Washington	4.6	38	57	5
Hartford-Louisville	1.7	13‡	81‡	6‡
Chicago-Indianapolis	17.6	28	65	7
Hartford-New York	10.3	58	30	12
Boston-Louisville	6.6	17	71	12
New York-Providence	18.0	69	15	26
Philadelphia-Roanoke	1.5	50	25	25
New York-Boston	167.0	25	48	27
Hartford-Washington	10.0	7	65	28
Hartford-St. Louis	5.4	70	1	29
New York-Washington	149.0	27	43	30
Boston-St. Louis	22.0	62	8	30
Baltimore-New York	13.2	9	55	36
Houston-San Antonio	8.7	15	44	41
Nashville-San Antonio	2.1	40	15	45
New York-San Antonio	52.0	4	45	51
Chicago-Cincinnati	22.5	32	13	55
Washington-San Antonio	20.3	9	35	56
Boston-Washington	67.0	11	17	72

Sources: * CAB. Domestic Origin-Destination Survey of Airline Passenger Traffic, Summary Data (1961).

† CAB. Competition Among Domestic Air Carriers, 3d Quarter 1961, unless otherwise noted.

‡ Same as note "†," but for 2d Quarter 1961.

pleasant to think that this spirit might come to imbue American Airlines after the merger, it is more realistic to note that American has not chosen to follow Eastern's step, in fact has ridiculed it, and might very well kill it. As has been suggested earlier, there is distinct public advantage in preserving as many independent competitors as possible; better to retain American and Eastern as rivals in route-markets already highly concentrated rather than bless their marriage because some competition would remain. All of the evidence, therefore, points to the conclusion that this merger will eliminate significant actual and potential competition as well as create monopoly on a number of routes.

The full implications of the American-Eastern merger cannot be appreciated, however, solely by looking at those markets where they presently are in competition. It is necessary to assess the significance of the fact that their consolidation will bring together the second and fourth

largest domestic trunk airlines and hence permit integration of their systems in such a way as to create a powerful new force within the industry. In a sense this will increase the extent of competition (in areas of low traffic volume); but it is more likely to divert traffic away from the weaker lines and hence further imbalance the industry. The reason for this stems from an analogy to the Gestalt effect—the whole being greater than the sum of the parts. Though they do compete over many routes, these two carriers by and large cover different sections of the country and can move traffic from any given location to any other on their unified system via any of 30 gateway cities. What this can mean, vis-a-vis other carriers, was noted by the CAB in 1946 when it refused to permit American to acquire Mid-Continent Airlines, the latter operating north-south from Minneapolis-St. Paul to Texas and New Orleans. The Board admitted that there was little direct competition between the two; but it feared that American, because of the great breadth of its operations, could undesirably distort the competitive situation in respect to the acquired routes. The Board explained:

[T]he wider the geographical scope of a carrier's operations in comparison with a particular rival, the greater the competitive advantage which it will enjoy through its control of traffic originating at or destined to points to which the other carrier does not have access. Because of this fact, the extension of a carrier's system may enable it to divert a substantial amount of traffic from a competing carrier without at the same time rendering a service more attuned to the public convenience and necessity.¹¹⁹

The way in which this can work is easily seen. Braniff Airways, for example, now carries a considerable volume of passengers to points on its system which originate at points served by Eastern Air Lines. In many cases American Airlines could destinate the passenger just as well as Braniff. But at the moment Braniff has an equal opportunity with American to secure this traffic. When the merger takes effect, however, it is reasonable to expect that most of this kind of business would be internally "captured" and routed entirely over the combined entity. The significance of this is apparent when it is noted that in January, 1962, alone, Braniff received revenues of about \$1 million just for service it gave to points on its line, also served by American, that was originated by Eastern.¹²⁰ Many similar examples could be recited, but their lesson would be precisely the same: when two major airline systems are consolidated, the tendency is to deprive other transporters, equally capable of providing the service, of the opportunity. This would be true of freight traffic as well. On cargo now moved between California and points in the southeastern United States the Flying Tiger Line (an all-cargo domestic operator) now provides much of the service; but upon their merger it is anticipated that much of this business would be taken over by American-Eastern.¹²¹

¹¹⁹ 7 C.A.B. 365, 378-79 (1946).

¹²⁰ Exhibit BN-10. American seeks to rebut this fear by showing the number of passengers who could have completed their trip via American but did so via Braniff. Exhibit AE-1250. The point has some merit, but with the far greater range of coverage held by a combined American-Eastern it is rather obvious that Braniff has a far greater risk of loss, both relatively and absolutely.

¹²¹ Exhibit FTL-1. In 1961 about 27% of the Flying Tiger Line's interlined freight was with Eastern; but since American is competitive with FTL over most of the latter's routes, the preponderance of this freight can be expected to move via American-Eastern.

The contemplated merger would also make possible new, through-service between many cities which presently require at least a single change of planes. This is a mixed blessing, offering some public advantage (though not as much as might at first appear) but raising the spectre of unjustifiable competition over routes which American Airlines itself would otherwise consider too limited in traffic to justify. To take the rosier side first, some 553 city-pairs could receive their first single carrier connecting service as a consequence of the American-Eastern merger.¹²² Not all of these, of course, will actually receive this service for the simple reason that they develop far too little passenger volume. In fact, of the 553 city pairs, only 39 offer more than an average of one passenger per day in each direction. The following are among the more important points that would receive their first single-carrier authorization:

Detroit—Nashville
 Cleveland—Montgomery
 El Paso—Miami, New Orleans
 Charlotte, N. C.—Tulsa, Oklahoma City, El Paso
 Huntsville—Los Angeles, San Francisco
 Los Angeles—Raleigh (and other Carolina points)
 Phoenix—Atlanta, New Orleans, Mobile
 Oklahoma City—various points in Florida
 San Francisco—Atlanta, Raleigh

In short, after the merger, if the service is actually made available, a passenger could fly aboard the same plane from Detroit to Nashville (not necessarily nonstop), or the other points indicated, where a change of planes (and airlines) must now be made. There is undeniable public improvement in this possibility, though it deserves emphasis that the city-pairs which are in this category involve relatively few people (the largest, Detroit-Nashville, averages only 12 passengers a day in each direction).

Furthermore, the merger would also permit direct, through-plane service between a number of cities already receiving service from at least one other carrier. It is this possibility that presents the greatest danger—threatening to harm seriously a number of weaker airlines and to enhance the American-Eastern industry position. All of the markets so affected provide significant amounts of passenger traffic, but far below the volume generated on routes where American Airlines presently insists competition is unjustified. Here is a list of some of the city-pairs which American-Eastern could serve directly on a through-plane basis that already receive nonstop service from another airline:

Atlanta—Los Angeles, San Francisco
 Miami—Los Angeles, San Francisco
 Jacksonville/Orlando—Los Angeles, San Francisco
 Birmingham—Los Angeles, San Francisco
 Charlotte—Los Angeles, San Francisco
 Caribbean (San Juan)—West Coast points
 Detroit—Memphis
 New Orleans—West Coast points

¹²² For an indication of the kinds of new service the merger will permit, see exhibit BER-1 and the American-Eastern response to the CAB's Bureau of Carriers Information Request No. 20, p. 1.

In each case American-Eastern would be required to make one stop en route and in some situations this would require some deviation from the most direct path (this, though, would not exceed about 100 miles).¹²³ How important these modest restrictions would turn out to be cannot be accurately predicted; carriers required to stop en route competing against nonstop rivals usually are disadvantaged, but American, apparently because of the goodwill and customer loyalty it has established, seems able to do well in spite of such conditions. Indeed, if the merger is approved, American plans immediately to inaugurate jet service between most of the points indicated above—some evidence of its own confidence in denting the markets.

Where the merger is likely to have its strongest competitive repercussions is along the Southern Transcontinental Route, the subject of awards by the CAB in 1961.¹²⁴ At that time the Board chose National Airlines to provide a nonstop service from Miami to California (with authorization also to serve Houston and San Antonio) and granted Delta permission to fly nonstop from Atlanta to California. In doing so the Board deliberately preferred these weaker carriers to American, which had vigorously sought either or both of these certifications. In commenting on American's application the Board said:

The fact of the matter is that the grant of American's application for an extension to Florida, coupled with its existing system, would give that carrier a southern transcontinental route. Obviously, the impact of this award to American would be such as to thwart the strengthening of Delta and National which was the objective of our awards to those carriers.¹²⁵

Put more straightforwardly, little more than a year ago the CAB expressly chose weaker carriers to provide service on the southern transcontinental routes; it deliberately excluded American; yet if the pending American-Eastern merger is approved without restriction American will have gotten, through the back door, exactly what it was refused at the front. Actually it appears that one of the major reasons why American favors the merger with Eastern is the expectation that this will give it the right to provide through service across the entire southern tier of states.¹²⁶

¹²³ This can have an impact in other areas and under other conditions as well. Consider the situation in respect to service between Washington and Minneapolis. Northwest, though authorized to fly nonstop between these points, actually operates only one such flight a day (it feels that traffic is too light to justify more than this). A combined American-Eastern could operate through-plane service between the two cities via Chicago and thus compete on almost an identical basis with Northwest, in spite of the fact the latter has a superficially stronger award. See exhibit NWA-A, pp. 5-6, NWA-136.

¹²⁴ Southern Transcontinental Service Case, 1A Av. L. Rep. ¶ 21,131 (1961).

¹²⁵ Southern Transcontinental Service Case—Supplemental Opinion and Order on Reconsideration, 1A Av. L. Rep. ¶ 21,171 (1961). Pertinent also is the decision of Oct. 30, 1961, in which the Board disapproved a lease agreement between American and Eastern calling for an interchange of equipment at Chicago that would permit through-plane service between Florida and California. The Board felt this arrangement would conflict with its Southern Transcontinental decision. Eastern Air Lines, Inc. and American Airlines, Inc.—Lease Agreement—Order Disapproving Agreement, 1A Av. L. Rep. ¶ 21,222 (1961).

¹²⁶ Recently the Court of Appeals for the District of Columbia set aside last year's CAB award of the Dallas-Florida segment to Eastern, on the ground that it was not supported by reasons and evidence that appear on the face of the record. Presumably the Board will again reach the same decision on remand. But changes in circumstances might lead to a different result, and conceivably the Board could thus prevent a merged American-Eastern from gaining a southern transcontinental route. Wall Street Journal, May 25, 1962, p. 6, col. 4.

The effect of the American-Eastern merger, therefore, would be to add a strong new carrier to routes which, just a year ago, were felt by the CAB to be best served individually by weaker trunklines. As one looks at the traffic data there is considerable evidence to support the Board's decision to confine through-carrier service along the southern transcontinental routes to a single carrier. By comparison with most of the more prominent markets in which competition was increased after 1955, the southern tier markets are noticeably thin. For example, in 1955 the Board opened up the Dallas-New York route to a second carrier; but this is a sizeable market, developing 168 million revenue passenger miles in 1960. By contrast none of the southern transcontinental routes generate this much traffic; here are some examples, with traffic for 1960 expressed in millions of passenger miles:

Houston—Los Angeles	38.0
Atlanta—Los Angeles	32.7
Atlanta—Dallas	15.0
Dallas—Los Angeles	77.4
Miami—Los Angeles	91.4

The two most heavily traversed routes thus produce only about half the traffic that moves between Dallas and New York; and of these two, one (Dallas-Los Angeles) is already competitive. Yet in each instance cited a merged American-Eastern could provide additional, through-plane service. Precisely what impact this would have is not easily determined. But the CAB's Bureau of Economic Regulation has estimated that the merger will divert \$7.4 million from National Airlines and an additional \$6.2 million from Delta, primarily as a result of service possibilities along the southern transcontinental routes.¹²⁷

There are other ways in which the merger might permit the parties to expand their market position and exert their influence beyond what is indicated simply by their consolidation. Some of these are difficult to assess; their precise impact on other, smaller competitors is incalculable. A few can be recited for purposes of illustration. For one, there is little doubt that American possesses substantial good will and traveler acceptance that gives it an advantage over rivals, even where their service is comparable. A large part of this, of course, may merely be due to its far more extensive advertising and promotional efforts.¹²⁸ Moreover,

¹²⁷ Exhibits BER-5/6. The Bureau of Economic Regulation estimates that a combined American-Eastern would gain approximately \$41 million in additional passenger revenue as a result of the merger. Of this amount \$23 million would come from service in the southern transcontinental area and \$18 million from other areas. Of the total amount roughly \$17 million would represent diversion from other carriers—the larger portion from National and Delta due to their extensive operations along the southern transcontinental routes.

¹²⁸ During the year ended Sept. 30, 1961, American spent approximately \$6.1 million on advertising, Eastern, an additional \$5.5 million—in each instance more than any other airline except United-Capital. On an available seat mile allocation, however, American spent only about half as much as the smaller eight. Exhibit BER-25. While a combined American-Eastern may save up to \$3.5 million in advertising outlays over the sum of their separate expenditures (exhibit AE-H-2), the other carriers are strongly of the view that the merged entity will have the merchandising upper hand. See exhibits CAL-16; DL-50 ("it is a generally accepted fact that the biggest carrier with the largest advertising budget and greatest exposure to the traveling public has the inherent ability to attract more passengers in any given market"), p. 2. The argument of the smaller companies comes down to saying that the bigger rival gets proportionately more "effect" for its dollar outlays. For other illustrations of this position, see Edwards, *Conglomerate Bigness as a Source of Power*, in National Bureau of Economic Research, *Business Concentration and Price Policy* (1955).

American and Eastern together account for some 66% of the cards outstanding under the Universal Air Travel Plan;¹²⁹ this tends to provide them with readier sales access to those business travelers who account for over 25% of passenger revenues collected through this credit system. In the larger cities, served by more than a single airport, the giant airline also would have a distinct advantage. In New York, for example, American and Eastern operate through all three of the city's terminals. This means that a passenger, arriving at one of the airports and required to change to another airline to finish his journey, more probably will select American for this completion leg than some other, smaller airline which also supplies the service but which operates from another airport. As an example: someone flying from a medium-size New England city to New York's La Guardia field, for onward movement to Detroit, will find that Northwest Airlines operates only from Idlewild and Newark. American, however, which likewise provides service between New York and Detroit, operates from all three fields. The typical passenger is quite likely, therefore, to select American over Northwest.¹³⁰ And the merger will insulate this process, offering more service to more points.

The potential advantage of American-Eastern is perhaps most readily seen through an examination of its equipment pool. By the end of this year, for example, American-Eastern would have about 31% of the country's jet fleet. In conjunction with the seasonality of their operations—American with peak demand in the summer, Eastern in the winter—rather clearly the merged company will be in a position to increase substantially the amount of service already being given on routes which they serve. In the winter, for instance, Eastern could literally flood the New York-Miami route with jet flights—far in excess of the number that its two competitors could offer.¹³¹ This would give it a marked advantage, for it is well-established that the carrier offering the larger number of flights typically becomes the market leader.¹³² In fact, this is already true on the New York-Miami run, ostensibly because of Eastern's more frequent service. This would be greatly accentuated in the event of merger with American. To listen to the pleas of the two airlines, however, one would think that in each other's off-season, the unnecessary flight equipment would be put in storage; this they admit is not contemplated, which implies that they will use the equipment to provide stepped-up service over

¹²⁹ UATP contracts are entered into between individual airlines and contracting concerns. Though the cards supplied can be used on any participating carrier, all transactions are handled by the original contracting airline. American reportedly makes duplicates of bills it renders and turns them over to its sales personnel; aggressively exploited this can be of advantage in offering assistance in reservations, planning or adjusting flight departure times, etc. The other airlines feel that American, in particular, gains many benefits through its dominant role in the UATP. See exhibits DL-50/51; BER-26; BN-A, BN-6/7.

¹³⁰ See exhibits NWA-130 and NWA-A, pp. 6-7. The gargantuan size of new terminals also tends to give the airline providing through-plane service an advantage over those which provide an interchange service requiring a change of planes. At Chicago's O'Hare field, for example, a passenger transferring from American to Northwest must proceed nearly $\frac{1}{2}$ of a mile; accordingly the minimum connecting time differential between a scheduled arrival and departure at O'Hare is now 50 minutes. To the passenger who can do so, therefore, it is faster to go via the through-service airline; this could reduce over-all flight time by at least 30 minutes.

¹³¹ And Eastern is known for taking just this kind of action. In 1959, for example, it distributed a memorandum, marked "confidential," which outlined "a positive offensive action of smothering the competition with schedules." Exhibit DL-36D, p. 1.

¹³² The close correlation between the number of flights offered and the share of traffic carried is shown in exhibits BER-11/15.

higher-volume routes. The impact of this on the weaker carriers is obvious; either they would be forced to acquire additional equipment, at a higher cost than American-Eastern pay in the capital market,¹³³ and with a consequent rise in capacity (something hardly to be encouraged), or have their share of the relevant markets appreciably reduced. This ability to shift a massive, diversified equipment fleet from area to area indeed appears to be one of the merged company's greatest sources of strength. Its exertion can only reasonably be expected to enlarge the consolidated airline's place in the market beyond that which merger alone would confer.

Mention of the internal advantages of a large equipment pool, however, raises a crucial question: might not a merged American-Eastern, because of its greater size, not represent a substantial gain in efficiency, with the lower costs inuring in some way to public advantage. This is simply a variant of the old theme: aren't the biggest companies the more efficient? The answer is no, whether it be steel or airlines. Those who have looked closely at the problem conclude that airline efficiency correlates, not with the size of the firm, but with exogenous factors, particularly the density of the route and the average length of haul. The Koontz¹³⁴ and Wheatcroft¹³⁵ studies have found few, if any, economies of scale beyond the level attained by the medium or medium-small companies. Moreover, beyond the middle-size range significant diseconomies appear to set in. Thus in 1960 TWA and American Airlines ranked, respectively, first and second in average length of hop (reflecting their generally longer flights), and third and first in passenger load factor; still they held only the fifth and seventh places in terms of total operating expense per available ton mile.¹³⁶ It is indeed a mistake to think that size and efficiency are directly related; they are not. Other factors are more important, and at some point size may become a disadvantage—in terms of efficiency although it may be useful to the possessor. A merger of American and Eastern would unite already large carriers; in some respects it would permit fuller exploitation of existing traffic; but more generally it would link together carriers with noncompetitive routes and hence contribute little to more favorable operating circumstances. In short, it promises little in the way of increased operating efficiency.

American and Eastern claim that their merger will permit other kinds of economies which make their consolidation meritorious. Merger, they insist, will permit the elimination of duplicate terminal and ticket facilities, allow consolidation of hangars and repair centers, reduce capital requirements, etc. The table below summarizes the claimed pretax savings:

¹³³ As of December 31, 1961, the average interest cost on outstanding debt of the biggest three airlines (excluding TWA) was 4.52%; for the seven smaller airlines, 5.41%. Exhibit DL-32, p. 1. Eastern has been able to borrow from major New York banks at attractive interest rates. Presently it has outstanding \$80 million in such bank loans. Of this, \$60 million is due 1963-65, bearing interest of $\frac{1}{2}$ of 1% above the prime commercial rate; \$20 million is due in 1964, bearing interest of $\frac{1}{4}$ of 1% above the prime rate. Eastern Proxy Statement, March 12, 1962, p. 37.

¹³⁴ Koontz, *Domestic Air Line Self-Sufficiency: A Problem of Route Structure*, 42 Am. Econ. Rev. 103 (1952). He found that only four of the airlines, at the time of his study, were at a serious cost disadvantage on account of their size. Of these, two have since disappeared (Colonial and Inland) and one, Northeast, in spite of CAB attempts at resuscitation, is bankrupt. The other, Continental, has been substantially improved in recent years through new long-haul awards.

¹³⁵ Wheatcroft, *The Economics of European Air Transport*, ch. III (1956).

¹³⁶ Exhibit JI-1, p. 34.

TABLE 10. AMERICAN-EASTERN, CLAIMED SAVINGS
AS A RESULT OF MERGER

Item	Amount of Savings (in thousands)	
	1962 level	1964 level
Depreciation		\$ 8,269
Interest		5,796
Advertising	\$ 3,000	3,500
Electronic Data Processing Requirements	906	2,792
Flying Hours Saved	13,037	14,379
Rentals and Utilities	3,586	7,862
Management Overhead, Outside Services, and Other Common Station Savings	11,000	12,100
	<u>\$31,259</u>	<u>\$54,698</u>

Source: Joint Response to Bureau of Carriers Digest No. 32, second rev., p. 1

Unquestionably these economies are impressive, if realized. How realistic they are remains open to serious doubt, however. Both parties currently use ticket and other facilities that are held under long-term lease—as in the case of terminal and hangar leases at O'Hare Field in Chicago, for example, that do not expire until 1998.¹³⁷ In such a case it is doubtful if any real savings can be affected. There are other similar examples, but all suggest that it will be a good deal more difficult to achieve as many savings as are claimed. Moreover, some of the savings were in reach before the merger was agreed to. For instance, of the \$13 million reduction in flying costs that is forecast, more than 92% comes from a reduction of 39,003 ramp hours in the use of Eastern's Constellation equipment. But Delta Airlines, in its intervening argument against the merger, contends that of Eastern's 76,000 ramp hours on this type of equipment in 1961, 60,000 could have been eliminated without merger simply through more intensive equipment utilization.¹³⁸ While this counter-claim itself is open to question, it raises some considerable doubt as to the extent of the economies that will actually be achieved as a result of merger.

In some respects, however, it is rather amazing how few the economies will be. Eastern and American state they now have firm contracts calling for the delivery of 65 Boeing three-engine jet 727 transports. Merger will permit this number to be cut, but by only six in number, rather modest indeed.¹³⁹ This evidences either an unspoken belief by the parties in a rise in passenger traffic over the near term or the small amount of benefit that the merger will actually bring about.

But to the extent the merger does represent possible dollar savings, one is struck by the great extent to which these economies could be realized *without outright consolidation*. Where the two airlines presently operate, e.g., separate ticket offices in a given city, it does not require merger of their corporations to achieve joint use of common facilities. In fact, already Eastern and American share a ticket office in the Statler Hotel in Dallas. There are probably similar examples elsewhere, and there is no reason why this simple arrangement could not be extended widely.

¹³⁷ Eastern Proxy Statement, March 12, 1962, pp. 19, 23. There are other similar illustrations.¹³⁸ Exhibit DL-37D, p. 1.¹³⁹ Aviation Week, May 28, 1962, p. 41.

American and Eastern will combine their hangar requirements at Dallas in the event of merger; but this could be done anyway. And in fact why could this sort of practice not encompass several airlines? Recently a number of airlines announced they had created a spare parts pool, which offers savings of over \$2 million annually. This could readily be extended to hangars, repair facilities, ground equipment (such as tractors, loading devices, etc.), and even perhaps to terminal check-in and processing operations. One indeed wonders why Eastern Air Lines requires a \$14 million passenger terminal of its own at Idlewild, and American another valued at \$21 million. It does not require clairvoyance to suggest the wisdom and practicability of having joint terminals, akin to the union stations operated by the railroads in major cities. After all, a man and woman can economize by sharing the expenses of driving to work without getting married.

C. Summary

All factors considered, and admittedly they do not all point in the same direction, the American-Eastern merger has little to commend it and much to recommend its rejection. Its consummation would significantly increase the overall level of concentration within the airline industry, a combined American-Eastern accounting for at least a third of total passenger traffic. Within a number of markets the competitive effect would be even more severe. Between several cities American and Eastern now provide the only service; merger would clearly mean monopoly in these cases. Over still other routes, where one or more other carriers are in competition, American-Eastern would clearly be the dominant airline, carrying more than two-thirds of the traffic in many instances. Moreover, due to the advantages possessed by the merged entity, particularly the ability to shift a massive, diversified equipment fleet from route to route, the long-run result would probably be to increase American-Eastern's share of the market at the expense of the industry's smaller airlines. Consequently, their consolidation would run counter to the Board's past decisions dealing with mergers (particularly as reflected in the *United-Western* and *American-Mid-Continent* acquisition cases) as well as to its recent policy of increasing competition within the industry.

It is true, however, that while the contemplated merger would kill some competition, in some areas it would increase the degree of competition. While this generally is a desirable quality, it is important to note that the markets affected in this case—largely lying within the southern tier states—are predominantly of low traffic yield. Only a year ago the CAB determined they were too small to support two competitive services and acted deliberately so as to prevent American from gaining a southern transcontinental route. It bears re-emphasis that American Airlines has argued with particular vehemence that the cause of recently depressed airline earnings lies in excessive competition. Yet the very markets which American suggests are unduly competitive generate far more traffic than the bulk of the markets where the American-Eastern merger would mean the addition of a particularly strong competitor. Moreover, although American insists that excessive competition is primarily responsible for recent airline financial troubles (a matter disputed earlier), its merger with Eastern goes only a very short distance in alleviating the condition.

For the sake of curtailing competition between a number of high-density markets in the upper Atlantic seaboard area and a few elsewhere the merger would bring together two large carriers that generally are not in direct competition with one another. Thus, even assuming for the sake of argument that the American argument is valid, the contemplated merger does not represent its concrete application. American indeed seems to have fallen between two stools. It can't have it both ways; nor, for that matter, can the CAB.

Of the substantial dollar savings claimed by the parties to the American-Eastern merger (and there is some considerable doubt whether they can be completely realized) the great preponderance can be achieved without outright consolidation. To combine ticket sales offices, or hangars, or terminal loading equipment, or spare parts, or most anything—including flight equipment itself¹⁴⁰—a merger is unnecessary. What economies the American-Eastern merger holds out thus can largely be accomplished *without merger*. Accordingly, as long as merger means, as it does here, the loss in some competition and the risk that the level of concentration will be still further increased, it is difficult to come to any other conclusion than that the planned consolidation is, to paraphrase the words of the statute, inconsistent with the public interest.

IV. CONCLUSION

Whenever an industry is beset by financial troubles a search begins for the devil. Commonly "excessive" competition fills the bill and mergers provide the means of exhortation. This is no less true of the airlines—their officials and regulators—than of other industries. To those seeking a simple, quick "solution" corporate consolidation indeed represents a temptation difficult to resist. Closer analysis suggests, however, that undue competition is not the culprit, that more fundamental, more elusive factors provide the explanation and that a cure for the airlines' plight will require more reflection, more information and above all more imagination than has heretofore been displayed either by the carriers or their government overseers. Under such conditions it would be the gravest of errors to think that mergers will, as a general matter, provide any lasting answer. Their approval, as the pending American-Eastern amalgamation well demonstrates, would lessen competition and threaten to increase the prevailing degree of concentration without offering any significant public benefits that could not otherwise be achieved.

Although the domestic trunk airline industry has suffered notable financial troubles in recent years (though less serious than commonly portrayed), the available evidence, fairly interpreted, suggests strongly that the near future will record substantial improvements. So far this year passenger traffic has been increasing at a rate indicating about a 10% rise in revenue miles compared with 1961. Although the load factor continues to fall, the greater operating efficiency of the jet along with the slackened pace of equipment acquisitions indicates that the current traffic

¹⁴⁰ There are many examples of equipment interchange and lease arrangements. See, e.g., New York-Houston Interchange Case, 16 C.A.B. 602 (1952). Generally, Winkelhake, *Interchange Service Among the Airlines of the United States*, 22 J. Air L. & Com. 1 (1955). Interestingly the Board itself, at an early date, recognized that an interchange of equipment might be acceptable where an outright consolidation would not. Compare United-Western acquisition, *supra* note 106, with United-Western interchange, *supra* note 115.

increases will lead to substantial profits for the industry as a whole during the current calendar year. And as long as the economy continues its upward movement, there is excellent reason to believe that 1963 will be an even better year. Looking back, if there is a single leading explanation for the industry's recent decline in earnings it is the failure of passenger traffic to grow since 1959 at the rate recorded in prior years. This, in turn, is related in part to the 1960-1961 recession and in part to the sharp fare hikes which have been placed in effect since 1958 (up by roughly 25% during the past four years). If the airlines' generally overzealous purchases of jet equipment is also considered, it is fair to say that much of the financial problem stems from their own miscalculations.

To place the blame for the decline in earnings on "excessive" competition, as many of the leading airline and regulatory officials are doing, hence seems particularly inappropriate. No doubt the increased competition stemming from the CAB's route awards of the last seven years has accentuated the problem. But it has not been an efficient cause. Recession, heavy investment in jet aircraft coupled with the high costs of introduction, a general decline in traffic at least partly the result of fare hikes, and a miscellany of other factors (e.g., work stoppages due to labor disputes) can far more reasonably be identified as the explanations for slackened airline earnings. And, despite a lack of comment on the point from within the industry, some of these forces are not beyond the influence of the carriers. Reliable evidence indicates that traffic growth correlates with airline fares and that raising fares only curtails the traffic essential to financial success. Thus economic wisdom here clearly calls for markedly lower fares capable of attracting the attention of the 80% or more of the American people who have never traveled aboard a commercial airliner. This seems to be the proper next step for industry action, with the Continental proposal of an economy rate 25% below the coach fare a good point of origin.

All things considered, mergers offer little of real benefit. While in some ways they would inhibit competition, this does not appear to be the cause of the airline industry's troubles. To sanction mergers in this context therefore, would be primarily to deprive the public of a quality that offers substantial advantages. Although rivalry here is of a limited variety, nevertheless there are compelling arguments for preserving as large as possible a number of independent competitors. Not only has experience shown this as leading to a wide range of important service and equipment benefits, but it has contributed to price advantages as well (Eastern's air-shuttle and air-bus innovations are examples, as are some of the novel fare offers of National). The creation of monopoly and the substantial lessening of competition is too big a price to pay for the achievement of so little.¹⁴¹

But to discount heavily the utility of mergers as a "solution" to the airlines' financial difficulties (to the extent those difficulties may not be

¹⁴¹ Among the other writers who share this general conclusion are Healy, *The Merger Movement in Transportation*, 52 Am. Econ. Rev. 436 (Supp. May 1962); Maclay and Burt, *Entry of New Carriers Into Domestic Trunkline Air Transportation*, 22 J. Air L. & Com. 131 (1955); Keyes, *A Reconsideration of Federal Control of Entry Into Air Transportation*, 22 J. Air L. & Com. 192 (1955). But there are those who are concerned that the prevailing degree of competition in the industry may be unwise and unwarranted. See Frederick, *Commercial Air Transportation* 180-181, 195-202 (4th ed. 1955); Gill and Bates, *supra* note 64, at p. 631; Koontz, *supra* note 134, at 123-24.

only temporary), is not to say that certain kinds of action should not be taken immediately to improve the industry's financial prospects. First, the airlines should begin immediately to experiment with markedly lower fares—sufficiently far below the prevailing levels and kept in force for a period long enough to permit reasoned assessment of their market effect. The CAB should encourage this action and not be disturbed if the fares charged do not cover fully-allocated costs; it can usually be presumed that the airlines will not provide service at rates below the incremental operating expenses incurred.¹⁴² It bears emphasis too, that such fare experiments should be conducted before a serious consideration is given to the curtailment of competition (whether via merger or otherwise), not after, as Chairman Alan Boyd recently implied.

Second, the airlines, prompted by the CAB, should immediately seek out new ways of reducing costs through joint facility operations. It continues to make little sense for the various airlines, individually, to operate ticket offices, maintain hangars, and so forth, when these can be easily shared. This seems particularly true in the case of functions less "visible" to the public. One recent step involved the pooling of spare parts. That could be extended to hangars, repair facilities, and other behind-the-scenes operations. Joint use of electronic data processing equipment for reservations and related purposes is clearly feasible; indeed it appears that Eastern's EDP facilities are more than ample to take care of both its own and American's needs as well. Interline leasing of flight equipment already is common; the principle deserves wider appreciation. Unquestionably there can be a large reduction in overall airline costs without the very substantial loss in competition that consolidations of the various companies would inevitably entail.

Third, the CAB should immediately undertake a study to determine how much the trunk airlines are losing through their operation of service along various low-density routes. Indications are that these losses are substantial and hence, if reduced, might ease the airlines' economic situation considerably.¹⁴³ Northeast Airlines, for example, contends that if it is allowed to abandon service to seven small New England airports it can save from \$1 million to \$1.5 million a year.¹⁴⁴ There are similar indications contained in the efforts of other airlines to give up service to selected low-volume points; American Airlines is presently seeking to suspend its operations at such places as Akron, Ohio; Douglas, Arizona; Midland/Odessa, Texas; Joplin and Springfield, Missouri; and Peoria, Illinois.¹⁴⁵

¹⁴² The more enlightened airline officials know full well that if additional traffic provides sufficient revenue to cover the out-of-pocket expenses incurred, it can be worthwhile—contributing to the payment of diverse overhead charges. The CAB, however, seems intent on requiring a given service to cover all costs. See *supra* note 98. This unwisely inhibits the very kind of promotional pricing that the Board and others advocate. See, e.g., the Report of Project Horizon, *supra* note 15, at 190-95.

¹⁴³ In 1956 the Air Transport Association acknowledged that many points served by the trunk airlines are truly unproductive and, absent enrichment from other routes, would require subsidy. Finding that to avoid subsidy a given location must enplane at least 57 passengers per day (which seems rather high), the ATA concluded, for example, that one-third of the points served by American in the last half of 1955 represented losses. For the other airlines the proportion was even higher: 61% for Braniff, 53% for Delta, 43% for TWA and United. Hearings Before the House Antitrust Subcommittee, Monopoly Problems in the Regulated Industries: Airlines, 84th Cong., 2d Sess. (1956), vol. 3, pp. 1653-55.

¹⁴⁴ Wall Street Journal, May 23, 1962, p. 13, col. 2.

¹⁴⁵ Joint Response to BC Information Request No. 31, p. 22.

Some suggest that one of the major reasons for Eastern Air Line's troubles has been its unwillingness to abandon a large number of points that generate revenue far below the probable related costs. In fact, on occasion Eastern has remained in competition with subsidized local-service carriers.¹⁴⁶ At this juncture, however, no one is certain of the magnitude of the losses involved in trunk line operations to such small-volume locations; this should be determined.

It would seem only wise to permit the trunk airlines to abandon service with far greater freedom than they have at present. To force the trunk carriers to provide service in cases where local service airlines would be subsidized is absurd. This only means that the richer routes (and the travelers involved) must provide sufficient profits from which the cost of unproductive service can be recouped. As well, this makes it more difficult to sustain competition in the bigger markets.¹⁴⁷ Let it be admitted that service abandonments by the trunk lines means that many communities would have to depend on feeder carriers for their air service and that subsidy payments might have to be increased.¹⁴⁸ This should not be alarming; economic common-sense dictates that if markets do not provide sufficient revenue to cover the costs of a given service, they can rationally only be served (and that appears to be the Congressional demand) at a price. And better that price be direct subsidy than that it be a hidden subsidy drained from operations in wealthier markets.

Fourth, the CAB should also begin a careful review of the various routes on which it has made additional competitive awards during the last seven years with a view to determining the adequacy of the traffic involved to sustain the existing degree of competition. Necessarily this would entail a specification of the Board's objectives in encouraging competition and a consideration of the effect of the increased traffic that most of the routes will generate this year. Such a review could give the Board a useful opportunity to consider the consistency of its actions in recent years. As was indicated in part II of this article, the CAB failed to take this kind of action at the time it made the various awards. The result is that there is little meaningful correlation between the number of airlines authorized to serve a given route and the level of traffic involved. Many incongruities are apparent.¹⁴⁹ Some routes with low traffic volume have been granted two unrestricted authorizations; others with even heavier traffic remain monopolized. Two carriers each serve St. Louis-Miami and New York-Dallas; yet in 1960 the former generated only about 25% of the revenue passenger miles of the latter. It would thus seem either that there should be more competition in some markets or less in others. At some point the Board should take its stand, publicly and explicitly spelling out its criteria. But until it conducts an inquiry of this type, in conjunction with a study of

¹⁴⁶ Some 73% of the stations served by Eastern that produced passenger revenue of less than \$1 million in 1961 were acquired subsequent to the original grandfather grants. Exhibit NAL-304. However, in 1961 Eastern disposed of its local-service type routes in upstate New York to Mohawk Airlines, a feeder carrier. (These routes had been acquired in 1956 by Eastern when it purchased Colonial Airlines.) Eastern-Mohawk Transfer Case, 1A Av. L. Rep. ¶ 21,200 (1961).

¹⁴⁷ See Richmond, *supra* note 64, at 253-56.

¹⁴⁸ Not necessarily, though. In calculating subsidy payments for local-service carriers the CAB now uses a so-called class rate formula which has the effect of submerging the results of individual station operations in overall system operations. See Local Service Class Subsidy Rate Investigation, 1A Av. L. Rep. ¶ 21,134 (1961).

¹⁴⁹ This matter is considered in detail by Richmond, *supra* note 64, ch. IX-X.

the matter of internal subsidization (outlined above) and its relationship to the question of trunk airline earnings, the Board cannot make intelligent decisions in respect to the tolerable level of competition. Even worse, lacking essential information and without a comprehensive policy, the Board might grasp at mergers as a way of easing the industry's difficulties. This would be a grievous error, for airline consolidations generally, that of American and Eastern in particular, promise to contribute little to the resolution of the industry's basic economic problems, yet are sure to deny the public the substantial advantages of competition.